

The political economy of compensation for nationalisation or municipalisation:

- national and international law and practice, and the implications for potential (re)nationalisation in the UK and elsewhere**

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1. Introduction

The potential cost of compensation is a significant factor in political decisions to nationalise or municipalise. The legal framework now includes not only national law, but also international treaties relating to investment and trade which provide for investor-state dispute settlement (ISDS) which may enable foreign investors to seek compensation through arbitration. These legal frameworks create expectations for investors of clear and quantifiable entitlement, but an examination of the law and actual practice shows rather an intensely political process between governments and business interests, with varying contested valuation principles, contested positions on national and international law, and strategic use of law-suits and arbitration by either party.

In the 2017 election in the UK the Labour Party announced plans to renationalise water, energy, rail and postal companies - the first time that a major political party has done so since the government of Mrs Thatcher privatised large parts of UK utilities. During the election campaign and subsequently these proposals proved to be immensely popular, with a major survey by a (right-wing) think-tank finding huge majorities supporting public ownership of water (83%), energy systems (77%), railways (77%) (Legatum Institute 2017, Labour Party 2019). This has led to a public debate on the advantages of public ownership of companies providing public services, of the desirability of ending PPPs, and of returning outsourced services to inhouse direct provision.

The main issue raised by investors and their advisors in this debate has been the question of how much compensation would have to be paid to the current private owners, and thus how much the policies would cost. The discussion concerns what is required or permitted under UK law, and especially whether it requires compensation to be based on the 'market value' of the company nationalised. Corporate law firms and others have been also talking up the possibilities for using BITs or the Energy Charter Treaty (ECT) to claim higher compensation. (Clifford Chance 2019, Macquarie 2018). These treaties are now being used more frequently by various investors against some high income countries in western Europe, especially under the ECT (TNI 2018), but at the same time there is a growing resistance to this use of the treaties: "the legitimacy of the international investment regime is increasingly questioned." (Hoffman 2018)

This paper considers both policy and analytical questions about national law and the international treaties. The policy question is whether investors can exploit these legal frameworks and practice to create a significant obstacle to the implementation of Labour party public ownership policies. The analytical question concerns the political economy of these legal frameworks and in particular the interaction of different actors and factors in the complex and evolving conflicts over the use of international treaties to claim compensation. It is structured as follows.

- Section 1: Introduction
- Section 2 analyses the framework of national law on compensation in the UK, and historical practice, and compares the legal framework in Germany and the USA.
- Section 3 concerns BITs and the ECT, and the potential relevance in the UK context.
- Section 4 concerns the interactions between governments, campaigners, investors, courts and arbitration tribunals over BITs, the ECT and FTAs.
- Section 5: conclusions

2. National law and practice

2.1 UK law and practice on compensation for expropriation

2.1.1 Legal framework: parliament decides each case

UK law allows and requires parliament to set its own rules for compensation in each specific case, taking account of public interest considerations, as determined by the democratic process. In each case there is an act of parliament which takes the relevant entities into public ownership and then “set out the terms of compensation for the property transfers and how this would be paid” (HoC 2018, Cairns 1951). Unlike the USA, there is no general right to compensation still less to compensation based on a specific formula or formulation, such as ‘market value’, and the London stock exchange rules for takeover bids have no relevance: “in England an owner is entitled only to what is accorded him by statute” (FRD 1949). Moreover, UK courts cannot overrule a decision of parliament.

The only relevant court cases have been those brought under the European Convention on Human Rights, which is incorporated into UK law, and none have been successful. Both the UK courts and the Strasbourg court have refused claims by investors that the amount of compensation was too low.

The basic principle was confirmed in 2012 by the UK Court of Appeal and the European Court of Human Rights (ECHR), in relation to the rescue of Northern Rock in 2008, where the shareholders were awarded zero compensation. Some shareholders brought cases arguing that this was unfair, because the share price was £0.90, not zero. However, these cases were unsuccessful: the evaluation process used by the UK government was validated as entirely legitimate by the High Court, the Court of Appeal ¹, and, for the same reasons, by the European Court of Human Rights. ² The UK Court of Appeal stated:

“the court would only interfere if it were to conclude that the State's judgment as to what is in the public interest is manifestly without reasonable foundation” ³

The ECHR re-stated the general principle that there was no right to full market value compensation if public interest objectives, including social justice and economic reform, lead to a different conclusion:

‘Legitimate objectives in the “public interest”, such as those pursued in measures of economic reform or measures designed to achieve greater social justice, may call for less than reimbursement of the full market value.’ ⁴

This is not a new doctrine. The same principle was stated by the English courts and the ECHR over 20 years previously, in rejecting claims for higher compensation by former shareholders of the shipbuilding and aerospace companies in 1977:

“A decision to enact nationalisation legislation will commonly involve consideration of various issues on which opinions within a democratic society may reasonably differ widely. Because of their direct knowledge of their society and its needs and resources, the national authorities are in principle better placed than the international judge to appreciate what measures are appropriate in this area and consequently the margin of appreciation available to them should be a wide one. It would, in the Court's view, be

artificial in this respect to divorce the decision as to the compensation terms from the actual decision to nationalise, since the factors influencing the latter will of necessity also influence the former.” (*Lithgow and Others v. the United Kingdom* (1986) 8 EHRR 329).⁵

It was also used to reject a claim by the Duke of Westminster, the largest landowner in Britain, against a new law introduced by a Labour government in 1967 allowing leaseholders to buy freeholds at much less than the market value. The courts noted that:

“such legislation had been part of Labour Party policy for some years. It was regarded as a necessary social reform, required to right an injustice....”

and again, that, with ownership of property as well as with shares,

“Legitimate objectives of 'public interest', such as pursued in measures of economic reform or measures designed to achieve greater social justice, may call for less than reimbursement of the full market value”. (*James and Others v UK* [1986] 8 EHRR 123) ⁶

This basic structure of the law was correctly summarised by the credit-rating agency Moodys in a 2017 paper on the Labour party proposals:

“ The level of compensation would fall within the wide discretion of parliament, and it is by no means certain that RAV [regulated asset value] is the value parliament would choose. We note that, in the nationalisation of Northern Rock, the European Court of Human Rights (ECHR) found [in 2012] that “legitimate objectives in the 'public interest', such as those pursued in measures of economic reform or measures designed to achieve greater social justice, may call for less than reimbursement of the full market value.” (Moodys 2017)

Three key points emerge:

- The basis for compensating shareholders is decided by government and parliament on a case by case basis, taking account of a range of relevant matters, including public interest objectives, and the particular circumstances of each case.
- the courts have consistently confirmed that public policy considerations are paramount, and that there is no general right for investors to be paid full market value as compensation. ⁷
- It is not true that compensation to shareholders must be based on the stock market value of the shares, or the enterprise value, or reflect stock exchange rules on private takeovers.

2.1.2 UK practice: compensation for expropriation

There is a long history in the UK of expropriation and nationalisation used as an instrument of economic, social and colonial policy, even before the nationalisations of the 20th century. Indeed, all property rights in the UK originate from the seizure by king William I of all land in 1066, and its subsequent distribution; and property rights in the USA derive from similar seizure of lands by the USA government, mainly without compensation (Singer 2011). Major historical events involving expropriation include the dissolution of the monasteries, the enclosure of the commons, the abolition of slavery, and the takeover of India by the British state from the East India Company.

The dissolution of the monasteries by Henry VIII in the 16th century involved the expropriation of the monasteries themselves and their sale or assignment to private individuals. No compensation was paid to the multinational monastic orders which owned the monasteries, but the state did provide pensions to thousands of monks, nuns and other workers (Pound 1986)⁸.

The enclosure of common land in the 17th, 18th and 19th centuries was carried out mainly under a series of acts of parliament, which authorised the enclosure by individuals of previously common lands totalling 2.8million hectares, about one-fifth of the entire land area of England. These acts authorised the enclosure but made no provision for people who lost their rights to the commons, despite campaigns for such protection which failed to overcome: “the obduracy of Parliament in refusing compensation” (Pound 1986, Neeson 1993).

The Abolition of Slavery Act 1833 ⁹ ended slavery in the UK and colonies (after 6 years of forced labour for existing slaves), and provided for public expenditure to compensate the slave-owners for their loss. The preamble of the Act combines the two objectives: “it is just and expedient that all [slaves] should be manumitted and set free, and that a reasonable Compensation should be made to the Persons hitherto entitled to the Services of such Slaves for the Loss which they will incur by being deprived of their Right to such Services”. There was nevertheless “substantial disagreement ... as to the mode and the amount of compensation” (Draper 2007). The Act specified that the total amount of compensation available would be £20million – equivalent to 40% of all government expenditure in that year, and to about £2.3billion in current values. Slave-owners submitted claims in respect of 800,000 slaves, valued according to market prices over the previous 8 years, and received compensation in the form of ‘perpetual annuities’ and undated government bonds paying 4%. These bonds continued to pay interest until 2015, by which time the descendants of slaves, as tax-payers, were paying compensation to the heirs of the slave-owners – though the slaves and their descendants received no compensation at all. (HM Treasury 2018)

In 1858 the UK government took direct control of India by expropriating the powers, territories, armed forces, rights and revenues of the East India Company, which had ruled India for the previous 250 years under a crown charter, but with a series of abuses. The company however continued to exist under the generous regulation of its charter of 1833, which included a government guarantee for the payment of dividends of 10.5% for 40 years, financed by the tax revenues from India. It was finally wound up by act of parliament in 1874, in which the government paid £200 for every £100 of shares, as had been guaranteed by the 1833 Act. Payment was made in cash or in government bonds paying 3%-4%, so that even after the company’s collapse, the shareholders could still enjoy a return of 8% on their original investment for the indefinite future – not far below the 10.5% which had been guaranteed by government since 1833. The payments totalled £12million (about £1.3billion at 2018 prices), and the bonds issued to pay the compensation were added to the debt of India, so that the interest on that debt continued to be paid by the people of India for another 70 years: “the Indian people are virtually paying dividends to this day on the stock of an extinct company in the shape of interest on debt”. (Robins 2012, quoting R.C. Dutt) ¹⁰

Two features of these episodes are of relevance for understanding later practice, current policy, and the political economy of compensation.

Firstly, the weakest groups do worst in terms of compensation. The nationalisation of India was accompanied by compensation for the former private owners, but not for the Indians who had suffered at their hands; the abolition of slavery compensated the slave-owners but not the slaves. In relation to the enclosures too, the commoners are given no rights to compensation for their losses. Parliament could have required such compensation, given that the purpose of the nationalisations in the slavery and India cases was to end abuses, but chose not to.

Secondly, the Slave-owners and East India cases introduce a striking new policy, that is the provision of compensation to property-owners which preserves their previous returns into the future,

financed by taxpayers through public debt. Again, there was no compulsion to be so generous, and considerable controversy over the awards, but the political strength of the slave-owners and the company shareholders prevailed.

The series of 'modern' nationalisations starts in the 1870s, but, consistent with the legal framework, the actual compensation has been determined by parliament in a political process in which owners and investors have pressed hard for whatever approach would maximise their compensation. This has not necessarily meant supporting a simple formula, such as the share price: e.g. the shareholders of an aircraft company taken over by the government in World War II argued that the actual share price of their company was the *wrong* basis for valuation, and the owners of steel companies renationalised in 1968 similarly argued that the share price woefully understated the value of their companies. (Cairns 1951).¹¹

- The telegraph companies were nationalised by the Conservative government under Disraeli 1870, which then made them part of the Post Office. The private telegraph companies were operating a cartel, disliked by businesses and by the press who paid for transmission of news, whereas the post office, which had already diversified into running a savings bank was seen as a model efficient bureaucracy by Gladstone and others. Compensation was paid on the basis of 20 years of profits – implying the perpetuation of a 5% return - which was criticised as unnecessarily high, but still worthwhile because of the public benefits (Perry 1997)
- In 1912 the telephone networks were also nationalised under the post office, this time by a Liberal government, for similar reasons to improve efficiency and remove problems of oligopoly. The Post Office already regulated the sector and under an agreement of 1901 “had the right to purchase the assets of the private companies without any additional payment for goodwill when their licences expired in 1911”, when the assets, rather than the companies, were duly purchased for £12.5m. and the sector taken under the control of the post office (Scott 2011).
- The creation of a public water company for London, the Metropolitan Water Board, in 1902 was also carried out by parliament, taking over the eight existing private water companies. After more public controversy, the act itself adopted the slave-owners' formula, that compensation had to be

“based on the cost of reinvestment to achieve a similar return... [which was]... almost double the total capital on the company books... The MWB used its borrowing powers as a public-sector entity to replace equity paying 10 per cent with long-term debt paying 3 per cent, but the amount of compensation was so huge that the Board started its life with a “*millstone around its neck*”.... which burdened the new public company, and thus its customers, with paying the same excessive profits as before”. (Goldsmith and Carter 2015)

This episode is especially illuminating, as it shows the continuation of the rule adopted for the slave-owners and the East India stockholders in achieving long-term perpetuation of their pre-nationalisation profits at the expense of the public ratepayer. It also draws attention to the long-term cost consequences of this policy.

- The nationalisation of industries following World War II adopted various methodologies, surveyed by two contemporary review articles and a more recent parliamentary report (Cairns 1951, FRD 1949, HoC 2018). In each case there was an act of parliament authorising

the specific nationalisation, and containing specific provisions for compensation to authorise the public expenditure involved. Owners were compensated with government bonds, which then became debt of the new publicly owned entities, but the amount was determined in various ways:

- Where companies were listed on the stock exchange, as with some electricity, gas, and transport companies, the value was based on the share price in the immediately preceding period.
 - The act nationalising the Bank of England specified that shareholders should receive the amount necessary to give the same return as the dividends previously enjoyed by shareholders – roughly four times as great as the face value of the shares (Cairns 1951)
 - with the nationalisation of the coal mines, which were largely privately owned, the assets themselves were nationalised, a single total figure of £165million was fixed for compensation, and then allocated to the owners according to comparative valuations of the assets
 - Local authorities were compensated with a lump sum reflecting the debt they had taken on to finance their undertakings such as in electricity and gas, and for recent capital expenditure, plus a total of £5million for loss of revenues,
- The survey by FRD summarised the various methods and outcomes as an attempt:
- “to express, in payment, an accurate equilibration between the rights of owners and the needs of the public..... The novel and varied measures adopted in making compensation for nationalization may be said to represent legislative decisions as to what extent the public interest justifies less (or more) advantageous terms of payment than might have been accorded under former principles.... It must be remembered that in estimating the "fairness" of compensation there must not be an identification of *fairness* with some absolute idea of what owners are entitled to receive for their property under all conditions. Rather it should be considered whether the legislature, in coming to its conclusion, gave the proper importance to each of the relevant factors.” (F. R. D. 1949)

A number of conclusions can be drawn in relation to UK law and practice on compensation

Firstly, any act of parliament passed under a future Labour government nationalising any companies would include a section providing for compensation, and this is exactly in accordance with UK law and practice on how compensation is determined. It is misleading for corporate lawyers to claim that “any nationalisation would be subject to legal frameworks that did not exist in the 1940s or 1970s. Legal challenges are therefore inevitable, particularly over the amount of compensation.” (Clifford Chance 2019) UK law has not changed at all, and it provides no role for the courts, apart from the ECHR cases, which have always been unsuccessful because the courts will not even consider interfering unless the decision can be shown to be “manifestly without reasonable foundation”. The decision-making process for compensation in the UK is, simply, the political machinery of parliamentary democracy, as part of which owners make their case – with a remarkable degree of success, historically. Indeed, the booklets published by corporate lawyers, stockbrokers and right-wing think-tanks clearly represent early participation

by investors attempting to influence this political decision-making process. The potential use of arbitration by foreign investors under BITs or the ECT is a separate issue, which is considered in a later section.

Secondly, the corporate lawyers' claim that there is an 'international norm' in OECD countries for paying what investors claim to be 'market value' is also a misleading picture. The next part of this section examines the law and practice in Germany - where a very recent and high profile case has resulted in a parliamentary decision to offer compensation on an utterly different basis from the 'market value' claimed by three multinationals – and the USA, where even the constitutional right to 'just compensation' is mediated through political processes and contested evaluations.

Thirdly, the arguments about the level of compensation must be conducted on their own merits. Nothing in UK law states otherwise, and there are multiple reasons why basing compensation on 'market value', or the preservation of past returns, is both economically harmful and inappropriate for re-nationalisations. The appropriate basis for compensation in these cases should rather be to return to shareholders the equity they have actually invested in the companies, enabling them to re-invest elsewhere exactly the same money that they have invested in the companies being re-nationalised. The final part of this section sets out such an approach in more detail.

2.2 Other countries and cases

2.2.1 Germany

German law on compensation is also based on its constitution, but the principles are significantly different from those in the US constitution. Article 14 (3) of the German constitution rules that expropriation is only permissible 'for the public good' and that it can only be done by a law which also "determines the nature and extent of compensation". It does not however specify any unilateral rights for investors to receive 'market value' or even 'just compensation'. Its only requirement is for a balance between public and private interests:

"Such compensation shall be determined by establishing an equitable balance between the public interest and the interests of those affected."

It also specifies that, like the USA but unlike the UK: "In case of dispute concerning the amount of compensation, recourse may be had to the ordinary courts". The centrality of 'balance', however, means that the fixing of compensation is not centred solely on perceived investor losses, let alone some notion of market value, but also on the impact on the public interest (German Constitution 2019).

The application of this principle was recently tested by the electricity companies who sued the German government for compensation over the decision in 2011 to compel closure of all nuclear plants. Germany had previously adopted this policy of nuclear phase-out in 2003, but intensive lobbying by the companies resulted in a decision in October 2010 for indefinite postponement of the closures, a decision in which "Important aspects of the law were negotiated rather than founded in fact" (Polk 2011). Then, following the Fukushima nuclear disaster in Japan, the original decision to phase out by 2020 was reinstated in March 2011.

The electricity companies with nuclear generators - E.on, RWE and Vattenfall - sued for compensation in the German federal constitutional court (FCC) in November 2011, arguing that the government's action was unconstitutional and that they were entitled to a sum as large as €19 billion Euros in compensation.¹² The court ruled in 2016 that, firstly, the nuclear phase out is constitutional; but, secondly, it was subject to article 14 of the constitution and so compensation should be provided; thirdly, however, the FCC refused to decide the value of compensation itself, and instead ruled that the parliament had to pass a bill by 2018 to regulate the compensation payable. In 2018 the parliament passed an amendment of the nuclear law allowing for 'adequate financial compensation for so-called frustrated investments the companies made in nuclear power plants between 28 October 2010 and 16 March 2011', but without specifying a precise sum, arguing that it will not be possible before 2023 to decide on an amount of compensation as only then will the amount of electricity not produced as a result of the frustration of those investments be clear enough to calculate the lost profits of the companies.¹³

However, the actual investments made in the 5 month period were probably close to zero, and so, even after a ruling by the constitutional court and a legislative amendment as required by the court, compensation could be close to zero and still meet the constitutional requirement for balance: "can be considered proportional even without compensation provided to the affected operators" (Bernasconi-Osterwalder and Hoffmann 2012). It also notes a number of other factors that may mitigate against the companies' claim: the fact that the companies capital has been almost fully amortized "reduces the need for protection of the operators"; that article 14 "does not protect the expected profits of the operators"; that state subsidies for the nuclear power stations, worth €203.7 billion between 1950 and 2010, could be taken into account; that the operators had to expect at least a very high risk of nuclear plants being closed from 2003 onwards, and so the risk was already factored into their business. (Bernasconi-Osterwalder and Hoffmann 2012). As the only foreign-owned company, Vattenfall is also seeking to use the Energy Charter Treaty to sue for compensation in front of an arbitration tribunal in New York. This ECT case is discussed below in section 5.

2.2.2 USA

The law and practice on compensation for nationalisation or municipalisation in the USA¹ is not a straightforward matter of rigorous application of a simple formula for 'full market value', and the determination of compensation is invariably settled through political mechanisms following procedural rules. The 5th amendment of the US constitution states: "nor shall private property be taken for public use, without **just** compensation", which provides a basis for legal action over compensation, and the courts have ruled that "the general standard is the market value of the property, *i.e.*, what a willing buyer would pay a willing seller". This is a significant difference from the UK, where there is no such basis for legal action. But the courts have recognised that there is no simple objective way of calculating 'fair market value' – especially in cases where a business, as opposed to land, is being expropriated. This allows for a wide range of different approaches to be used, and the states have created procedures to be followed in determining compensation when entities are taken into public ownership. (Legal Information Institute 2019)

¹ In USA legal terminology, the power of governments to expropriate property is known as 'eminent domain', and the act of nationalisation or municipalisation is known as 'takings' or, confusingly, 'condemnation'.

This is not just a theoretical issue in the USA. Contrary to common assumptions, public ownership is widespread, at municipal, state and federal level. Indeed, in the sectors targeted by the UK Labour Party – water, energy, rail, and postal services - the USA has a higher level of public ownership in 2019 than the UK. About 87% of water supply services are owned and run by municipalities; there are about 2000 municipally owned electricity utilities – including cities such as Los Angeles - serving about 49million people, or 15% of the population, as well as the federally owned Tennessee Valley Authority, which supplies 9 million people. There are hundreds of municipally owned ports, airports and public transport systems, a thriving bank owned and run by the state of North Dakota, and more than 750 publicly owned internet networks with speeds, service levels, and costs as good as or better than commercial systems. At federal (national) the US Postal Service remains 100% owned by the government – unlike in the UK and some other European countries – as well as the passenger railway system Amtrak and various financial institutions such as the mortgage financiers known as Fannie Mae and Freddie Mac, which are both in the top 10 largest financial corporations in the USA by revenue (Hanna 2018 , APPA 2019 , Fortune 500 2019).

As elsewhere, there have been trends towards re-municipalisation, and so the question of compensation arises regularly. There have been over 70 cases of re-municipalisation of water supply since 2003, most of which have taken the form of recreating a municipal service after the expiry of a private concession, but at least nine were cases of municipalisation by ‘eminent domain’ of existing private companies, including the case of Missoula discussed below. There are fewer cases in energy, but this may change: in 2019 the city of San Francisco published a report which concluded that “public ownership of San Francisco’s electric grid has the potential for significant long-term benefits relative to investment costs and risks”; city councillors in Chicago have called for a feasibility study on municipalisation of energy when the current 28 year old concession expires in 2020; and, amidst multiple failures in the private electricity supply to New York City, the mayor warned that “we need to think about some kind of public approach”. (Ulmer and Gerlak. 2019 ; San Francisco PUC 2019 , APPA 2019)

A 2012 survey of the laws on the process and methodology for fixing compensation in relation to the municipalisation of electricity utilities shows wide variation in procedures, and acceptance of multiple methods of calculating value of compensation, both between states and even within states. With regard to the process, the great majority of states expect the amount to be fixed ‘by agreement’, with various other mechanisms available if no agreement is reached. Many states refer the decision to the Public Services Commission (the regulatory body in most US states), but some allow the use of citizen juries, including Alaska, Florida, Idaho, Louisiana, Michigan, North Carolina, Tennessee, Utah, and West Virginia, which emphasises the political nature of the process. Where valuation methods are referenced, they vary widely, as in Alaska, where: “Courts have accepted multiple valuation methods in eminent domain proceedings to determine just compensation, including fair market value, replacement value, and reproduction value”. (Briggerman et al 2012)

There are two important ways in which USA practice does not follow the investors ideal . Firstly, some states depart sharply from corporate notions of market value (and some of the UK practice) by explicitly excluding any account of future earnings. In Massachusetts “the Department of Public Utilities (DPU) is required to determine what price should be paid, having in view the cost of the property less a reasonable allowance for depreciation and obsolescence, and any other element which may enter into a determination of a fair value of the property so purchased, **but such value shall be estimated without enhancement on account of future earning capacity or good will, or of exclusive privileges derived from rights in the public ways**”; in Alabama, the PSC “determines the

fair value of the assets based on cost less depreciation, plus severance damages, **but not taking into account future earnings, good will or certain real estate rights**, and deducting or withholding the value of encumbrances, pending discharge thereof". Secondly, the constitutional right to just compensation does not enable investors to endlessly repeat the same arguments in the hope that the judges will award a more favourable formula than the political process. If compensation has been determined by following the due process of the relevant state "in some appropriate way, before some properly constituted tribunal"¹⁴ then "its findings as to the amount of damages will not be overturned on appeal"¹⁵ to the Supreme Court. (Legal Information Institute 2019A)

Some states reference other valuations made for other public purposes. In Idaho the court, jury or referee is expected to take account of "assessed value for property tax", and in Florida the PSC is expected to take account of "other items which are normally included in valuations of electric utility assets". This refers to the valuations of a company which are carried out under the USA system for regulating the rates that private utilities can charge to customers, where the valuation is used to calculate what kind of return is reasonable. In this field too, the myth of a precise formula has been rejected by the courts: "For almost fifty years the [Supreme] Court wandered through a maze of conflicting formulas and factors for valuing public service corporation property.....only to emerge by holding in *FPC v. Natural Gas Pipeline Co.*[185](#) that "[t]he Constitution does not bind rate-making bodies to the service of any single formula or combination of formulas". Indeed the Supreme court adopted a principle of non-interference - similar to the view of the UK courts and the ECHR - that the courts will not overturn a valuation unless the objector can prove it is manifestly unreasonable in its effects: "it is the result reached not the method employed which is controlling, . . . it is not the theory but the impact of the rate order which counts, ...and if the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry ... is at an end" and "he who would upset the rate order . . . carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences."¹⁶ (Legal Information Institute 2019; Merrill 2002 ; Briggerman et al 2012; Legal Information Institute 2019B)

The recent case of Missoula illustrates the political dynamics of the USA process (Mann and Warner 2019). In 2017, the City of Missoula, Montana, in the western United States, used its powers of eminent domain to take ownership of its water system from The Carlyle Group. The process involved a series of public sector actors - the mayor, judge, and Public Services Commission (PSC) – with a key role being played by 70% public support for "ending the flow of money to corporate owners in California and regaining control of their future" on the one hand, and information asymmetries, legal resources and effective 'capture' of the regulatory PSC favouring the company on the other hand. The city had to initiate a court case, which ultimately went up to the supreme court of Montana, in which it had to demonstrate that there would be better value for the public from the takeover, as well as arguing for its proposed level of compensation. The city argued in court that it should be \$46million, Carlyle argued for \$143million, and the final settlement was for \$88.6million. Mann and Warner conclude that: "Power asymmetries place municipalities at a disadvantage at every stage of the negotiation... Missoula's experience seems to point to an inevitable collision between private equity firms and the public, whose interests are nearly diametrically opposed."

These are clearly political processes whose outcome reflects the balance of economic and political power between the two parties. There is no golden formula at the end of the rainbow. As summarised by Merrill (2002):

"as astute observers have long recognized, the concept of fair market value is essentially a fiction in [this] context.... What actually happens in a case in which there is a dispute about

the measure of compensation? Basically, the condemning [public] authority introduces evidence, often through the testimony of expert witnesses, which tends to show that the property has a relatively low value. The owner then introduces evidence, often using rival expert witnesses, which follows one or more of these techniques and tends to show that the property has a relatively high value. The tribunal, which may include a jury depending on the jurisdiction, will then have to determine which evidence is most persuasive...; often, it will reach a compromise between the positions of the two parties. The number picked by the tribunal is deemed to be the "fair market value".

2.2.3 Other cases of compensation by negotiation

Other cases in both OECD countries and developing countries show a similar process of negotiated settlements. As in the USA cases, the initial claims of the investors function as an opening bargaining position, government evaluations are counter-proposed, and agreements are generally reached.

When New Zealand reversed the privatisation of its rail system in 2008: the NZ government first offered NZ \$350m., the private owners asked for over NZ\$1,150bn., but ended up settling for NZ\$690m: a little less than 2/3 of what they originally claimed as the market value.¹⁷

In 2013 the Welsh Government – which does not enjoy the same constitutional status as the UK parliament - nationalised Cardiff Airport by buying 100% of the sharers from the previous private owner, TBI/Albertis, a Spanish multinational. The private group initially asked for £200million; an evaluation commissioned by the Welsh Government estimated the airport was worth between £20m. and £35m.; the government then offered £41m., and the parties finally settled on £52m. A subsequent audit concluded that the Welsh government had paid too much.¹⁸

A slightly different process can be seen in Bolivia, which in 2010 nationalised the 50% of the electrical power station Guaracachi which was owned by Rurelec, a company listed on the London stock exchange. The subsequent process included use of arbitration by Rurelec under a UK-Bolivian BIT, which resulted in a tribunal award in 2014 of \$41million: but a few months later compensation was finally settled at \$31.5million, nearly \$10million less than the award, and less than half what the investors had claimed. In effect, even the BIT award was part of the process of reaching an agreed figure, rather than an external determinant of the level of compensation.¹⁹

Even the nationalisations in Venezuela by the government of Hugo Chavez show a similar picture of negotiated compensation. In contrast to the assertion by legal firm Clifford Chance that 'many of these nationalisations were effected without any compensation' (Clifford Chance 2019), the U.S. Ambassador to Venezuela in 2007, William Brownfield, spoke with approval of the 'rapid and seemingly amicable negotiations' and publicly stated that: "the negotiations seemed to respect investors' rights". The list of actual compensations paid, as reported by Reuters, show impressively large amounts of compensation, totalling at least \$6billion: the US multinational AES was paid \$739million compensation for the Caracas electrical utility, a deal which AES President and CEO Paul Hanrahan described as "fair and respectful of investors' rights"; Verizon were paid \$572million for their stake in the country's telecoms company; US energy group CMS got \$105million for their stake in a small electricity generator. Venezuela also paid \$2billion compensation for nationalisation of a steel mill, \$600million for a cement company, \$1billion for European stakes in oil companies, and \$1billion to Santander for a bank nationalisation.²⁰

A case in Germany shows how investors can obtain excessive compensation through ethically dubious networks and improper procedures. In 2010 the federal state (Land) of Baden-

Württemberg, then led by the rightwing party CDU, paid €4.7billion to buy a 45% stake the energy company EnBW from the French multinational EdF, whose CEO at the time was Henri Proglio. The state constitutional court ruled the deal unconstitutional because it was done without first consulting the parliament, and the CDU leader was advised only by the head of the German branch of Morgan Stanley, who exchanged emails about the deal with the head of Morgan Stanley in France, René Proglio, who happened to be twin brother of the EdF CEO.²¹

These are examples of negotiations in which investors have achieved favourable results. This is not always the case. In Chile, the 1973 military coup led by General Pinochet first occupied the offices of El Clarin, a Chilean newspaper which supported the elected government of Salvador Allende, and later expropriated it by decree: subsequent attempts to claim proper compensation under a BIT finally failed in 2017.²²

2.3 Conclusions

There is no reason to expect that legal action could be successfully taken under UK law, or the ECHR, if future nationalisations provide compensation based on returning to shareholders the actual amount invested by them in the companies, as measured for example by the book value of equity, rather than a measure of market value based on expected future earnings. In relation to the UK, the law allows parliament extremely wide scope.

The estimates of 'market value' which have been published by stockbrokers and commercial lawyers and others should thus be seen as an opening negotiating position by investors in a dynamic political process, rather than a serious attempt to forecast the final result of a legal challenge in the UK. Since the nationalisation has not happened, the impact of these estimates is through the media on voters and politicians: the contested issue is not any actual compensation, it is the policy itself. Since it is now accepted that compensation cannot be obtained through UK courts, the attention has switched to the potential under international treaties, discussed in the next section.

Secondly, a cross-country comparison of laws on compensation undermines any general theory of a 'universal' principle of entitlement to compensation of a specific kind. The law in the UK, USA and Germany differs in relation to the powers and duties of parliaments, courts and the rights of investors. More generally, practice across all countries shows a clear political process between two parties with conflicting interests, the public/state, and investors, with formulae and methodology as contested as any other element.

Thirdly, apart from the fundamental impossibility of a UK court overruling parliament, the two key reasons given by the UK courts for not disturbing parliamentary decisions each have echoes in the law and practice elsewhere. The UK courts' insistence that "Legitimate objectives in the public interest, such as those pursued in measures of economic reform or measures designed to achieve greater social justice, may call for less than reimbursement of the full market value", endorses the balancing of public and private interests that is explicit in the German constitution. And the refusal of the courts to interfere unless it can be proved that a compensation scheme is "manifestly without reasonable foundation", is echoed in the USA Supreme Court resistance to overturning state-level findings on the amount of compensation: in effect, the parliamentary process in the UK is treated as the equivalent of the 'due process' at state level in the USA. The German FCC's decision to refer the calculation of compensation to the Bundestag shows a similar deferral to political processes.

By contrast, the next section shows how international treaties neither recognise the relevance of the public interest, nor the validity of established democratic and legal processes.

2.3.1 Fair and balanced compensation: returning actual investment to shareholders

Debates about compensation are also debates about the policy of public ownership itself. This section sets out four principles for determining compensation for nationalisation. The amount of compensation resulting from these principles is certainly substantially lower than that which would result from a re-application of methods which use the concept of market value to guarantee future returns equivalent to past returns, because the principles recognise the public economic interest in public ownership and its conflict with the interests of investors. As the judges stated in the Lithgow case: “It would be artificial to divorce the decision as to the compensation terms from the actual decision to nationalise”.²³

A. Fairness to public interest

‘Compensation shall be determined by establishing an equitable balance between the public interest and the interests of those affected’.

The question of fair compensation for taking a company into public ownership involves fairness to two parties, and so the principle of balance should be central – as it was in the 1940s nationalisations (FRD 1949) and as is expressed in the German constitution (2019).

A fair level of compensation must therefore take account not only of investors interests, but also the public interest, including the public interest in “measures of economic reform or measures designed to achieve greater social justice”²⁴ which, in the words of the UK courts, may require less than the ‘full market value’ which investors typically claim. Fairness to the public requires that the economic and social benefits of these reforms should be delivered and not negated by the cost of compensation.

Fairness to investors should involve returning to them the actual money which they have invested in the service. They should get their money back.

B. Returning shareholders’ actual investments

Compensation should do no more than return to the private shareholders the actual net assets in the company financed by shareholder equity. No compensation should be paid for loss of expected profits, nor for any value derived from government subsidy or support or regulatory regime, nor for any value derived from sale of assets or avoidance of pension liabilities or underperformance of statutory or regulatory duties or avoidance of tax.

The companies in parts of mature public service systems which have been privatised are not comparable to companies operating in other spheres. Their business is entirely framed by the requirements and licenses structured by the state and its democratic structures, which determine the public objectives of the system and its economic framework, including requirements such as universal service and the standards to be met. They have not built up the business through their own initiative, nor had to compete in a consumer market with other companies, and their investments are not made on the basis of entrepreneurial risk in consumer markets.

The income and returns of these companies reflect their success in obtaining concessions, contracts, or acquisition of state-owned enterprises, and interacting with regulators and politicians to maximise those returns. The regulatory system usually has the objective of ensuring that companies are sufficiently profitable for investments, and may be ‘captured’ by the private companies to permit

higher levels of extraction. The actual returns of such companies are thus determined not by successful market activity but by successful political activity in obtaining supportive terms from the state through its public service structure.

The renationalisation of privatised public service operators or the termination of public service concessions or contracts should not therefore require compensation as though the company had been built by private enterprise in a consumer market. It should simply reflect the principle that investors are entitled to get back the money they have actually invested in the companies. The core measure of this is the net assets in the company financed by shareholder equity as shown in the company books. The process of determining how much to return to shareholders should also take account of all relevant evidence including, regulated capital less net debt, the extraction of value by various means, the extent to which shareholders' value has been based on state grants, their performance of their obligations, the financial responsibility of their management, reasonable expectation of risk management, and other factors.

The shareholders then get back all their actually invested net capital, and can invest it in any other enterprise of their choosing, without restriction.

C. No perpetuation of excessive or monopoly returns through 'market value'

Shareholders of companies brought into public ownership should not receive compensation which maintains for them the level of excessive or monopoly earnings or returns that they enjoyed during the period of privatisation.

The central objective of nationalisation or municipalisation of privatised utilities and other public services is to end the extraction of excessive returns by shareholders which are seen as excessive by public and their political representatives. Since these returns are typically extracted through monopolies or oligopolies or long-term low-risk concessions, it is economically more efficient to end such monopoly returns.

But the market value of companies is based on expected earnings, and enshrines the expectation of future continuation of those excessive and/or monopoly returns. The difference between the market value of a company and the book value of the actual shareholder investments in a company is, in accounting theory, determined by the extent to which the shareholders are enjoying 'abnormal returns' above the risk-free rate. (Feltham and Ohlson 1995). Paying market value as compensation thus defeats the main economic objective by enabling the private owners to continue to enjoy, even after nationalisation, the abnormal returns they had before nationalisation. As noted by the Financial Times city editor: "The whole aim of the exercise would presumably be to stop private companies from making excessive returns from the public. Why then would the government start by paying a market premium based on those same excessive returns?" ²⁵

It would impose on consumers of the service (or tax-payers) the burden of paying, through a future publicly-owned company, charges which include the cost of financing the excessive returns to the private investors even after they have ceased to own or operate that company. This cost is in effect the same as the cost of the excessive extraction of profits under privatisation, so no economic benefit is gained by the public. As with the compensation paid to slave-owners or the East India company shareholders, these costs could remain a burden on the public for decades.

Paying compensation based on preserving into the future the current returns of the owners of the privatised companies, whether through using some measure of 'market value' or otherwise, is also

economically inefficient. Firstly, it amounts to payment of a capitalisation of monopoly profits, and puts the investors into the privileged position of continuing to enjoy monopoly returns even after losing the monopoly itself. Secondly, in a globalised economy, any compensation paid may be invested or spent anywhere in the world, and so be lost to the national economy: compensation should be minimised, rather than maximised. Thirdly, it eliminates the major efficiency saving of reducing the cost of capital under public ownership.

D. Public discussion and democratic processes

The process of determining actual compensation should be fully public including audits, hearings, and debates to ensure that the public interest can be heard and represented both by elected politicians and by civil society organisations.

Outcomes can be expected to reflect the relative strength of political and economic interests, but the chances of achieving a fair balance between the public interest and investors are greatly improved through public meetings, published audits, and full transparency including a role for civil society organisations.

3. International treaties and potential relevance for the UK

3.1 Historical asymmetry of international law on compensation

Claims for compensation for expropriation of companies can also be made under international treaties which provide mechanisms for investor-state dispute settlements (ISDS). These treaties include bilateral investment treaties (BITs) between two countries, multi-lateral investment treaties of which the most relevant is the Energy Charter Treaty (ECT) and free trade agreements (FTAs) covering a particular region or trade between two or more states or groups of states. The ISDS clauses typically enable companies to take claims for compensation against states over expropriation or other actions diminishing expected returns, either to the World Bank's arbitration tribunal (ICSID) or to the International Chamber of Commerce (ICC) or to the United Nations Commission on International Trade Law (UNCITRAL).

Although these agreements are formally symmetrical, giving equal rights to investors from each country, they were always intended for use by western investors against developing countries. (Miles 2014, Wellhausen 2015). The BITs rather form the latest historical stage of a series of protection mechanisms for European and north American investors. Empires were the simplest method for providing this protection, but other mechanisms were used to avoid European or North American investors being subject to the rule of law in countries outside empires. These included the 'capitulations' agreed by the Ottoman empire from the 17th century onwards which exempted European traders from being subject to rulings of Ottoman courts (Ahmad 2000), and later 'gunboat diplomacy', whereby countries were threatened with naval attacks unless the claims of investors were met. A system of international law was developed in the 19th century, especially to protect USA and European investors in the independent Latin American countries. This was conceptualised as a universal law superior to the supposedly unreliable and 'politicised' legal systems of non-western countries: "only an international setting could be relied upon to apply universal rules and ensure a neutral, depoliticised, and fair hearing for a foreign investor" (Miles 2014 p.1007). In response, these countries developed the Calvo doctrine, which stated simply that "Aliens should be afforded no more than the same treatment as nationals, and must limit themselves to filing claims in the local judicial system". (Miles 2014 p. 1000)

BITs and ISDS mechanisms were created in the second half of the 20th century, to provide post-colonial protection for western investors after countries gained independence from empires, strengthen demands for compensation from nationalisations by socialist countries, and later to protect investors in east European countries in transition from Soviet communist states. The ECT was originally created to give west European and north American investors strong legal rights in the exploitation of Russia's energy resources in the post-Soviet era, though ironically it has not been ratified by Russia. As FTAs were developed from the 1980s to accelerate globalisation, they incorporated the same ISDS mechanism to give international companies and investors greater security. (Miles 2014, Ciocchi and Khoury 2018, TNI 2018). A similar post-colonial legal superiority can be seen in the asymmetrical conditionalities for development aid - for example in 2019 the USA is funding electricity reform and privatisation in Ghana, under a 'Power Compact' agreement which states simply that "this Compact, upon entry into force, will prevail over the domestic laws of Ghana." ²⁶

3.2 Continued asymmetry under BITs, ECT, FTAs

This asymmetry can be clearly seen in the tables below, which cover cases brought under BITs, the ECT or FTAs. Whereas investors from EU15/USA/Canada have initiated re have thus been very few cases brought against EU15/USA/Canada, and even fewer brought by investors from developing countries., bear this out.

Apart from the two Vattenfall cases discussed below, the UK, France, Germany and Netherlands have faced only 3 cases, two of which were brought by an individual Indian investor, whereas their own companies have initiated a total of 297 cases. Both Italy and Spain have received a number of challenges, mainly under the ECT against renewable energy schemes, but the vast majority of these have been from other EU15 or 'old' OECD countries: if the EU succeeds in ending all intra-EU actions under BITs or the ECT, such cases from other EU15 or 'old' OECD countries will no longer be possible. The figures for Canada and the USA appear balanced, but 27 out of the 28 cases against Canada have come from the USA, and 15 out of 16 cases against the USA have come from Canada, all under NAFTA, which has now been replaced by an agreement with no ISDS. With the exception of some of the recent ECT cases against Spain, hardly any of the challenges to have come from countries outside the EU15.

The reverse pattern is clear in the second table, setting out the activity of Asian and transition countries , including 'new' EU member states in Eastern Europe. Unlike the EU15 countries, they are targets twice as frequently as initiators. Even when they do originate complaints, 90% of cases are against other developing or transition countries. Turkey has been far the most active country on this list, but apart from the single case against France, and a failed case against Romania, all cases have been against non-EU/non-OECD countries. This pattern also extends to new EU countries like Poland, whose investors' challenges have focussed almost entirely on their neighbours in eastern Europe and the eastern Mediterranean, and even Ukraine, which has brought a number of cases but nearly all are against Russia, and the others against former communist neighbours.

And none of the handful of cases against an EU15/OECD country have yet been successful. Until Japan joined the flurry of ECT actions on renewable energy with 3 cases against Spain, the only cases ever brought by major Asian countries against an EU15/OECD country consist of two cases from an Indian individual in 2000 and 2006, neither of which even reached a tribunal hearing; the Philip Morris case against Australia which was thrown out (see below); a Chinese case against Belgium's bank rescues in 2012 and a Slovakian case against Greece's restructuring of bonds in 2013, both of which were rejected, and a discontinued Turkish case against France.

These patterns show a striking post-colonial continuity with the unequal relationships of empire and earlier trade and investment. The reaction by the German government and the EU against such cases can thus be understood as a reaction to the disruption of both a long-established colonial practice, and, with cases brought from other EU-15 countries, of a long-standing convention that these legal mechanisms are not to be used by fellow-members of the club of rich countries against each other.

Table 1. International disputes: largest EU/north American countriesSource: UNCTAD <https://investmentpolicy.unctad.org/investment-dispute-settlement>

Country	Cases as home state of claimant	Cases as respondent country	Of which:	
			cases brought by EU15/OECD countries	Cases brought by investors in other countries
France	49	1	0	1
Germany	62	3	2	1
UK	78	1	0	1
Netherlands	108	0	0	0
Italy	37	11	11	0
Spain	50	49	42	7
Canada	49	28	27	1
USA	174	16	16	0
TOTAL	607	109	98	11

Table 2. International disputes: east European and large Asian/African economiesSource: UNCTAD <https://investmentpolicy.unctad.org/investment-dispute-settlement>

Country	Cases as respondent country	Cases as home state of claimant	Of which:	
			cases brought against EU15/OECD countries	Cases brought against investors in other countries
China	3	5	1	4
Hong Kong	0	1	1	0
India	24	6	2	4
Indonesia	7	0	0	0
Japan	0	4	3	1
Korea	7	5	0	5
Malaysia	3	4	0	4
Singapore	0	4	0	4
South Africa	1	3	0	3
Turkey	14	33	1	32
Poland	30	7	0	7
Slovakia	13	1	1	0
Czechia	38	5	0	5
Hungary	16	1	0	1
Romania	15	1	0	1
Bulgaria	10	0	0	0
Ukraine	23	11	0	11
TOTAL	204	91	9	82

3.3 Relevance for UK proposed nationalisations

The potential use of these treaties against a future UK government have become part of the public debate on the nationalisation proposals in the UK. A recent FT report warned that “Labour’s nationalisation plans risk ‘flood of claims’: investors seeking compensation could bring lawsuits under bilateral treaties” , quoting commercial law firm Clifford Chance as expecting companies to use BITs or the ECT to claim compensation.²⁷ The debate of course is not about actual cases, but about whether the prospective cost of compensation is so high as to demand abandonment of the policy.

However, there are a number of reasons to doubt whether such a flood will materialise or have the desired effect. In a letter to the FT the following day, Professor Peter Muchlinski warned that ISDS was becoming ‘increasingly outmoded’, that tribunals may not accept relocations just to take advantage of ISDS, and that the threat of using ISDS to block popular re-nationalisations could provoke a national backlash against the firms and strengthen opposition to ISDS mechanisms themselves.²⁸ The report by Clifford Chance (2019) is also unreliable on matters of fact, e.g. stating that the UK has a BIT with India, which was in fact terminated by the Indian government in 2017²⁹; and suggesting that awards to foreign investors would lead to UK shareholders being given the same level of compensation, despite the fact that the UK courts and the ECHR have already ruled, in the *Lithgow* case concerning the 1977 shipbuilding nationalisation, that the payment of higher compensation to foreign investors did not give UK shareholders any rights to the same level.³⁰

As the tables above show, even one case would double the historic total of BIT cases against the UK, and represent a complete innovation in the use of BITs by investors based in Asian countries.

In terms of current eligibility, the biggest investors in UK water and energy companies from BIT countries are the Cheung Kong Infrastructure group (CKI), based in Hong Kong, the YTL group of Malaysia, and state-owned funds from China (CIC and others), Singapore, Abu Dhabi, Kuwait and Qatar. Together they own about 20% of both the water and the energy grid sector. In addition investors from countries in the Energy Charter Treaty (ECT) own about 13% of the energy grid companies, mostly held by investors from Spain (Iberdrola) and Germany (Allianz).

Only one of the relevant BITs specify ‘market value’ as the basis for compensation (Singapore). The China and Hong Kong BITs say simply ‘real value’; the Malaysian BIT just says ‘value’, and specifies that ‘the amount of compensation shall be determined by due process of law in the territory of the Contracting Party in which the investment has been expropriated’, which in this case is UK law: which does not look promising if the objective is to challenge the evaluations made under UK law. The ECT, however, does specify ‘fair market value’, as do the new FTAs with Canada and Singapore. But both of those new FTAs also specify that ‘valuation criteria may include going concern value, asset value including the declared tax value of tangible property, and other criteria, as appropriate’

Clifford Chance (2019) Apart from these existing investors, owners of shares in UK water and energy companies could in principle re-arrange their holdings via a BIT country. However, as Muchlinski points out, tribunals may regard such ‘treaty-shopping’ as an abuse, as happened in the case brought by the USA tobacco multinational Philip Morris against the Australian government, using a newly established subsidiary in Hong Kong to take advantage of a Hong Kong-Australia BIT (which also happens to be the only BIT case ever brought by a company based in Hong Kong). The tribunal threw out the case because at the time of the relocation of a holding company to Hong Kong there was clearly “a foreseeable dispute”.³¹ Tribunals may take a similar view of similar moves by UK

companies, especially since Clifford Chance have publicly recommended such relocations precisely because they foresee a potential dispute with a future UK government : “It would therefore be unsurprising to see some investors who do not have the benefit of an investment treaty moving their investments into entities attracting investment treaty protection and there are already reports that this is being considered.” (Clifford Chance 2019).

The prospect of cases under the ECT could also be relevant for the proposed UK nationalisation of the energy companies, but the relevant investors based in countries signatory to the ECT are in Spain (Iberdrola) and Germany (Allianz). Both of these countries, and the UK, are signatories to the Jan 2019 EU agreement not to use the ECT against fellow members of the EU (see below); the applicability of this agreement post-Brexit is uncertain.

The interpretation of the BITs and ECT is entirely in the hands of the arbitration tribunal, who are not bound to follow any precedent. In practice there is no consistent formula or definition even for assessing what is ‘fair value’ in each case, and so the scope for arguing over the actual method for calculating compensation is therefore wide. Certainly it can produce very generous results. In the Yukos case against Russia under the ECT, the final tribunal award accepted the argument that the compensation should include all the potential growth in value between the nationalisation and the tribunal decision, which increased the calculated compensation from \$11billion to \$33billion; one commentator observed that this: “does not put back the claimant in the situation in which they would have been, but transports them into a more desirable economic situation...” (Cazier-Darmois 2018).

The former north American free trade treaty, NAFTA, enshrined this variability in its definition of compensation: “Valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value” (NAFTA clause 11). Ironically, given the demise of NAFTA, CETA uses identical wording, and the EU-Singapore FTA likewise (except with ‘may’ instead of ‘shall’, which increases the acceptability of variations.)

Given these uncertainties, coupled with the fact that claims are not always successful, are always costly, and would certainly take many years, and with a growing hostility to the use of ISDS against western countries, discussed below, it may be considered unlikely that eligible investors will launch a ‘flood’ of compensation claims, if a hypothetical future Labour government does offer less compensation than investors want.

The key issue in this debate, however, is not predicting that hypothetical future, but assessing whether the present threats of such future BIT or ECT claims will affect the policy position of the Labour party. So far, the Labour party has firmly stated that it is not being swayed by such threats. On the contrary, they may even strengthen support for the public ownership policies if current owners announce they will leave the UK to avoid being constrained by its laws. The companies are aware of this risk, according to the FT report: “utilities have held back from restructuring their operations to secure BIT protection because of fears about reputational damage”.³²

4. Contesting ISDS: money, trade, sovereignty and democracy

Over the last decade there has been an escalation of conflict over the use of ISDS under BITs, under the ECT, or under FTAs, involving a number of actors with diverse political and economic interests.

The dynamics affecting these agreements include not only bi-lateral or multi-lateral deals between states or groups of states, but also national and international pressure from opposing economic interests. On the one hand they are driven by the lobbying by business groups, both through the 'national route' of lobbying states, the 'Brussels route' of direct lobbying of the European Commission, and a combined route of 'capturing' member states' representatives on EU committees. This is opposed by a public resistance to a globalised economy which delivers relatively little benefit to people, which sees trade agreements as undermining democratic controls over environmental and labour standards and the structure of public services (CEO 2019, Greenwood 2017, Dür and Lechner 2014, Dür et al 2019, Rodrik 2018)

These developments are summarised in the table below, and examined in greater detail in the following sections.

Table 3. Political economy of ISDS cases: actors, actions and conflicts

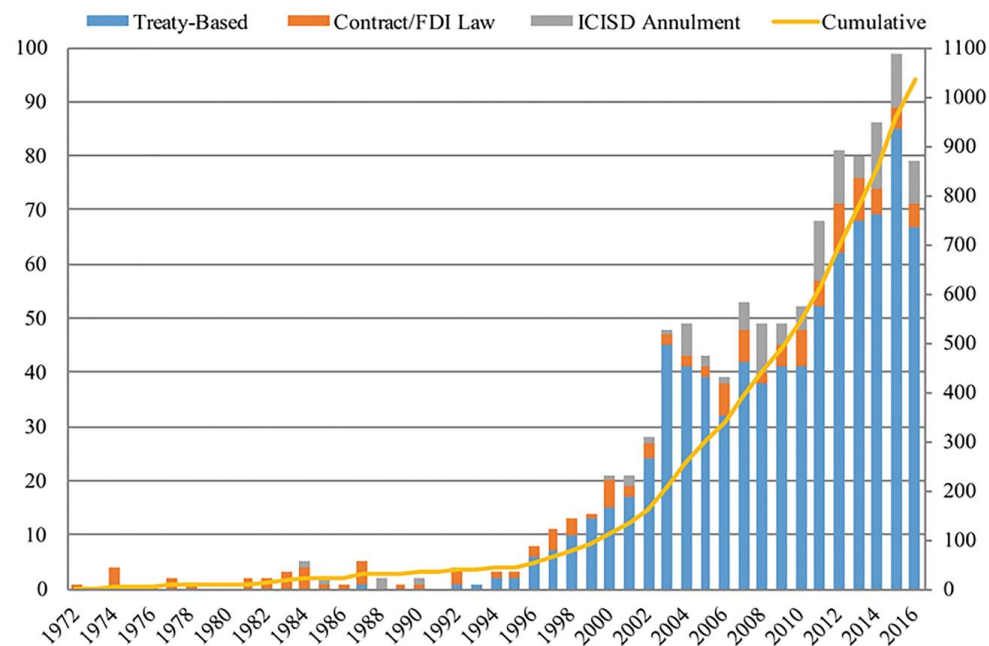
Actors	Main actions	Key factors
Investors	brought a wave of BIT and ECT cases against European countries, as well as elsewhere opportunistic relocations to countries with relevant BITs	Extra-judicial mechanism for claims Protect returns
Law firms	encouraged BIT/ECT cases to exploit the potential for profitable business	Commercial opportunities for lawsuits Oligopoly of arbitrators
Developing countries	Developing countries have started terminating BITs, including India, South Africa, Indonesia, Ecuador, Bolivia	Democratic/national policy decisions Sovereignty and Calvo principle Public service protection
Public campaigns	National actions against use of ISDS including court cases in Germany Successful global campaigns to eliminate or restrict use of ISDS in FTAs, e.g. defeat of TTIP, Global and national campaigns build public support.	Democratic/national policy decisions Environmental/labour regulation Public service protection Sovereignty and Calvo principle
USA and other OECD	USA under the Trump administration has withdrawn from FTAs with ISDS, including NAFTA, TTIP, CPTTP New FTAs have modified or abandoned ISDS clauses.	Nationalism Sovereignty Legacy protection for own investors overseas
European Commission and CJEU	Opposed developing countries initiatives to terminate BITs acted to nullify the use of the ECT e.g. ruling that some ECT awards are illegal state aid organised a remarkable declaration that they regard use of BITs or the ECT by one member state against another as contrary to EU law under the Achmea ruling, and have advised investors and courts that such awards are unenforceable continuing to sign new FTAs, some with ISDS provisions and some without	Continued protection for own investors overseas Commitment to maximising trade EU sovereignty over legal processes Sovereignty and Calvo principle

	as well as the renegotiation of the ECT, and the restructuring of ISDS through an 'International Court System'.	
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4.1 Investors and law firms and 3rd party funders

A key driver of conflict over ISDS has been the surge in cases brought under BITs or the ECT in the last decade, as shown in chart below.

Chart A. International investment arbitration cases registered by year (1987–2016).



Source: Langford et al 2017

A number of these cases have been based on intra-EU BITs, claiming compensation for policy changes by EU member states.

One such case involved a claim against Poland for cancelling the planned flotation on the stock market of PZU, the Polish health insurance company, which was jointly owned by the Polish government and a Dutch-owned company, Eureko. Eureko had expected to get another 21% of the company in this flotation, and so claimed, and won, compensation of €1.8 billion under the Netherlands-Poland BIT, which “allowed Eureko to get around a clause in the privatisation deal committing the two sides to adjudicate any disputes in Polish courts.”³³ The amount was so great that Poland had to ask to spread out payment to avoid speculation against the Polish currency (Hall 2010). A similar case involved a private company suing Slovakia for changing the regulation of health insurers; again, the company chose to go to arbitration using a BIT between Netherlands and Slovakia. This case, *Achmea vs Slovakia*, was later in 2018 ruled incompatible with EU law by the CJEU (see below).

There has also been a major surge in cases brought under the ECT: only 19 cases were brought in the first 10 years up to 2008, but 75 investor lawsuits were filed between 2013 and 2017. The cases are now being targeted at western European countries, principally Spain and Italy, with large claims: 16

cases involved claims of over \$1billion. Most claims come from companies registered in Europe, though many are ‘letter-box’ companies registered there for convenience, and a large majority of the cases against Spain, for example, are brought by financial investors. These claims have specifically targeted government policies in support of renewable energy, which has the effect of slowing down such policies by making them too costly.

The law firms are key actors in this, advertising the opportunities for litigation - “Five elite law firms have been involved in nearly half of all known ECT investor lawsuits” - which is further facilitated by third party funders who finance the legal costs in exchange for a share in any award (CEO/TNI 2018). The concentrated power of a small group of lawyers is intensified by their dominant position both as counsel to parties in the case and also as arbitrators. A group of just 25 lawyers have been appointed as arbitrators in 44 per cent of the ECT cases, and two-thirds of these have also been counsel in other cases. There is in effect an investment arbitration industry consisting of law firms, arbitrators and financiers who have vested interests in perpetuating and expanding the caseload. (Langford et al 2017, CEO/TNI 2018)

4.2 Developing countries terminate BITs

Countries in the Global South have long resented the use of BITs against them by investors from north America and Europe, and now a number of large economies have started terminating BITs.

Table 4. Developing countries reject or terminate BITs

Country	Actions
Brazil	Brazil never signed BITs, and now develops a new model of CFIAAs (see below)
Ecuador	ended BITs with 10 countries between 2008 and 2010 (Table 1) after new constitution in 2008, and in 2009 formally withdrew from the International Centre for Settlement of Investment Disputes (ICSID). In 2010, Ecuador’s Constitutional Court declared the arbitration provisions of six more BITs unconstitutional.
India	India gave notice in 2017 to terminate 58 BITs,
Bolivia	terminated 11 BITs between 2012 and 2014
South Africa	has withdrawn from all its BITs, including 9 BITs with European countries. ³⁴
Indonesia	announced in 2014 it would terminate all its 67 BITs

Sources: Public Citizen 2018, Martins 2017,

The action by South Africa was prompted partly by a 2008 claim by Italian mining investors for compensation of \$268million for South Africa’s implementation in the mining sector of black economic empowerment regulations, a key measure to reverse the economic and social injustices of apartheid.³⁵ The government was not prepared to accept such interference with crucial policies, and so terminated all its BITs. It argues that the South African constitution provides sufficient and equal protection for all investors.

A surge in cases brought by investors against India led directly to the government’s decision to terminate existing BITs, although it continues to seek negotiation of new agreements based on a

‘model BIT’ which still provides for ISDS and covers ‘indirect’ expropriation, and so is much weaker than the CFIAAs promoted by Brazil (see below) ³⁶

Brazil has never been a party to any BITs but still receives substantial amounts of foreign investment. The National Congress of Brazil has refused to ratify proposed BITs, and also refused to ratify the ICSID convention, because of the risks associated with the traditional ISDS system. Instead, Brazil has developed an alternative model of Cooperation and Facilitation Investment Agreements (CFIAAs), and has already signed such agreements with Angola, Chile, Colombia, Malawi, Mexico, Mozambique, and Peru. These CFIAAs focus primarily on cooperation and investment facilitation, and include specific social responsibility obligations on investors, based on OECD guidelines, including provisions against corruption and against destruction of the environment. CFIAAs cover only FDI – not financial investments, which may be simply speculative – and are based on the principle of giving foreign investors the same treatment as domestic investors. Compensation for expropriation is covered, but not ‘indirect expropriation’, which has been used under BITs to challenge democratic policies on infrastructure or services. There is no provision for ISDS, but each country has to create a national Ombudsman to resolve grievances, and ultimately for state-state conciliation or arbitration. (Martins 2017)

The termination of BITs does not lead to a fall in foreign direct investment. Ecuador, Bolivia, South Africa, Indonesia and India have terminated BITs, and foreign investment has still grown. (Public Citizen 2018)

4.3 Public reactions: the German cases

Public campaigns against ISDS in general and trade agreements in particular have been widespread, but the greatest impact on the politics of these instruments has come from Germany, as a result of two major campaigns.

The first was the huge reaction against the ECT case brought by a Swedish company to demand over €4 billion in compensation for the country’s decision to phase out nuclear power stations

The second was a constitutional court case against the EU-Canada trade deal CETA.

Both of these cases are still continuing at the time of writing (August 2019), but the political effects have already been great.

4.3.1 Vattenfall vs Germany

The largest ECT case anywhere in the world to date is the claim by the Swedish electricity multinational Vattenfall, which owns one of the largest electricity companies in Germany. Vattenfall has twice used the ECT to claim compensation from German public authorities, itself a remarkable fact, since only one other case has ever been brought against Germany under any international investment or trade treaty. The first case brought by Vattenfall was against the city of Hamburg over its environmental policy restrictions on a new coal-fired plant, which resulted in forcing a policy change to reduce these environmental standards (Jacur 2015).

The second and much larger claim was for €4.7 billion damages against Germany over the decision in 2011 to compel closure of all nuclear plants. The electricity companies with nuclear generators - E.ON, RWE and Vattenfall - sued first in the German federal constitutional court (FCC), but, as discussed in section 2 above, the process under German law is not expected to yield much compensation. So, in parallel to the legal proceedings in the German court, Vattenfall, as the only foreign company able to use international treaties, filed a claim under the ECT for €4.4 billion euros

compensation, at ICSID in May 2012.³⁷ After 7 years, as of August 2019, the case has still not been settled. Extraordinary amounts have been spent on lawyers during this long legal battle. By April 2018 the German Government had spent more than €15 million in legal and administrative costs to defend the case, and Vattenfall has spent €26 million on its lawyers, which it also claims from Germany.³⁸

The case has been widely criticised in Germany, and the government has made a strong resistance: in 2018 it submitted to the ICSID tribunal that Vattenfall, a Swedish company, could not use the ECT against Germany because of the CJEU ruling on Achmea (see below), and then it asked for the suspension of all 3 members of the ICSID tribunal: both proposals were rejected by ICSID.^{39 40} The German government also formulated a plan for a new international court system (ICS) to replace ISDS mechanisms, which has been adopted by the EU as a central part of its reform efforts.

Firstly, the ECT is being used to seek far more generous compensation than the process of German justice will deliver. It thus exposes the contradiction between the apparent symmetry of BITs/ECT, and the status of the legal systems in western countries: the German courts are being treated in the same way as western countries have treated the legal systems of south American or Asian countries.

Secondly, the German government and parliament have been extremely firm in resisting the ECT case, made it as difficult as possible for Vattenfall, and effectively increased the stakes to the point where any ECT award would be treated as a clear challenge to the authority of the German courts and parliament. This has undoubtedly influenced the remarkable 2019 declaration by EU states, see below, that the ECT should not be used by investors from EU countries against other EU countries, nor enforced by their courts. It is in effect an assertion by European countries of the Calvo doctrine, that foreign investors are entitled to justice under the national system.

Thirdly, the case has provoked such a strong reaction because it simultaneously attacks the status of the German legal system.

Schill's explanation of the strength of opposition to Vattenfall's case against Germany links it clearly to the impact on democratic decision-making: "The entire political and social landscape in Germany has been so deeply influenced by the struggle against nuclear power that Vattenfall II, and with it investor-State arbitration generally, is seen as a challenge to a fundamental social and political settlement and hence to democracy more generally" (Schill 2015)

4.3.2 The case against CETA: Germany and elsewhere

There have been strong campaigns against free trade agreements all across Europe, including Germany, because of their effects on democratic rights to determine policy and because of the power given to companies through ISDS provisions. The most important focus of campaigns was on the proposed deal with the USA, TTIP, and the proposed EU-Canada free trade agreement, known as CETA.

An intense public debate in Germany included a number of leading lawyers and others arguing that the ISDS provisions in these proposed treaties were incompatible with the German constitution, would give special rights to Canadian investors, allow secret tribunals to make binding decisions, and create a deterrent effect against social or environmental legislation or regulation. At one stage even Socialist party (SPD) ministers in the coalition government argued at one stage that ISDS was harmful and unnecessary, because foreign investors could use German courts, and the Bundesrat adopted a

resolution that neither TTIP nor CETA should include ISDS mechanisms (Bungenberg 2016). In 2016 German citizens submitted a constitutional complaint at the Federal Constitutional Court, with more than 125.000 supporters, the largest civil action in the history of the Federal Republic of Germany, asking for an injunction against Germany's political representatives agreeing to the treaty, because it violates the German constitution and restricts the right of citizens to determine their own political destiny.⁴¹

In October 2016 the FCC issued a mixed interim judgement.⁴² It ruled that the German representatives could agree to CETA in the EU Council - but that it was an agreement covering "mixed" competencies of both the EU and member states, and that any Council decision regarding CETA must only concern those parts of the agreement that undoubtedly fall within the exclusive competence of the European Union, so excluding Chapter 8 on investment and ISDS (and also the chapters on maritime transport, professional qualifications, and trade and labour. It also ruled that member states should be able to veto decisions by CETA committees, so that any conflict with the German constitution could be blocked. Finally, it ruled that CETA Art. 30.7(3)(c) has to be interpreted as to allow Germany to unilaterally terminate the provisional application of CETA, and that Germany should give clear public and international notice of this interpretation of CETA (Baumler 2016). The final ruling of the Federal Constitutional Court is expected in autumn 2019.

EU ratification of CETA has so far carefully respected this judgment. In February 2017, the European Parliament voted for CETA on the basis that it was a mixed agreement, which requires individual ratification by every EU country, including provision for domestic mechanisms for enforcing ISDS. Ratification by the German parliament awaits the final ruling of the Federal Constitutional Court.⁴³

A further outcome of the German process was the formulation by the German government in 2015 of a proposal to deal with some aspects of the legal status of the ISDS arbitration tribunals. Instead of ad hoc tribunals and arbitrators, there should be a permanent international investment court, with permanent judges. This was subsequently adopted as EU policy, see below, and the such a system is referenced in both CETA and the EU-Vietnam agreement, even though no such court yet exists (Bungenberg 2016).

CETA has also been the subject of intense campaigns in Belgium, and opposition by the Flanders region of Belgium delayed the Council approval of CETA, and then asked the CJEU to rule on the compatibility of CETA and its ISDS provisions with EU law. In May 2019 the CJEU ruled that CETA is compatible with EU law, because the tribunals/courts would only take account of EU law by accepting CJEU interpretations. Although it concerned only CETA, it implies a similar legitimacy for the other similar FTAs with Singapore and Vietnam, and for the EU-supported UN initiative to create a global investment court. Given the court's ruling in *Achmea* (see below) that member states may not use BITs against each other, the effect seems to perpetuate an odd asymmetry whereby a Canadian company could sue a government under CETA, but a company in the same situation, based in an EU country, could not do so.⁴⁴ The ratification by individual countries may yet prove problematic: by mid-2019 10 member States had ratified CETA or were "reportedly at an advanced stage"; Italy, however, has threatened not to ratify CETA as it considers that the protection afforded for labels of geographical origins is insufficient". Campaigns against CETA continue, with over 555,000 citizens signing an EU-wide petition against ISDS provisions in treaties.⁴⁵ The German FCC reasoning was based on preserving national legal competences, rather than the wider concerns over democratic policy-making, but it means that each member state can control the operation of the ISDS provisions, and it has inserted a right of unilateral termination. Both of these weaken the potential impact of CETA considerably.

4.4 EU reaction: not in our back yard

The EU reaction has been complex and tactically wide-ranging. On the one hand it has criticised developing countries for terminating BITs, and it continues to negotiate FTAs some of which include ISDS. It also seeks to create a new more legitimate international system of investor courts, and to renegotiate the ECT itself. On the other hand, it has urged countries to end intra-EU BITs, ruled that tribunal awards under these agreements are illegal state aid, welcomed a CJEU ruling that such BITs were incompatible with EU law, seeks to extend the ruling to cover the ECT, and has organised a declaration by member states that both intra-EU BITs and the ECT should not be used and will not be enforced by their courts. The EU has undoubtedly been influenced by the German backlash in many of these policies.

➤ **Some awards are illegal state aid**

In *Micula v. Romania*, a case brought by Romanian investors who had relocated to Sweden to use the Sweden-Romania BIT, the EC prohibited Romania from paying out a US\$250-million ISDS award for a breach of an investment treaty by an EU state aid decision, stating that payment of the award itself would violate EU state aid law. This was partly overturned by a CJEU ruling in 2019 that it could not apply to a period before Romania's accession to the EU. The Miculas have also initiated cases in 7 countries, including the UK and the USA, to order payment of the award.⁴⁶

The EU Commission has also ruled that some compensation awards made by tribunals under the ECT, for example against Spain over changes in its policies on renewable energy, cannot be paid because they constitute unfair state aid under EU law.⁴⁷

➤ **Achmea case: no BITs between member states, no valid ISDS**

In the Achmea case a company used a Netherlands-Slovakia BIT to claim compensation from Slovakia because it reversed the privatisation of health services. The arbitration tribunal awarded compensation to Achmea, but Slovakia referred the judgment to the CJEU, which ruled in March 2018 that the arbitration agreement in article 8 of the BIT has an adverse effect on the autonomy of the EU legal order and so is incompatible with EU law.⁴⁸

Following up on this judgment in July 2018, the European Commission stated that, if investments are affected by member state action, the investor can sue the member state in the national courts which have jurisdiction..... any tribunal constituted under an intra-EU BIT or the ECT (see below) lacks jurisdiction and '... national courts are under an obligation to annul any arbitral award rendered ... and to refuse to enforce it'.⁴⁹

➤ **BIT tribunals and other courts ignore Achmea and EU declaration**

The Achmea has not deterred tribunals subsequently hearing intra-EU ECT claims. In each of the awards rendered following Achmea, tribunals and national courts have either refused to be briefed on Achmea (Antaris) or dismissed the state's objections in reliance thereon (Antin and Masdar). Since 2018 tribunals have ruled:

- that the CJEU ruling in Achmea does not prevent the use of the multi-lateral ECT by EU countries against each other⁵⁰
- does not even prevent the use of claims under a BIT where the legal framework is ICSID rules rather than German law (as was the case with Achmea)⁵¹

- does not prevent the use of a Luxembourg-Poland BIT to claim compensation for losses by shareholders as a result of bank nationalisation. Arbitral awards in investment protection dispute remain mainly unchanged. ⁵²

➤ **EU member states declaration January 2019: no intra-EU use of ISDS under BITs or ECT**

The strongest action organised by the EU Commission came in January 2019 when the EU member states (including the UK) all signed a remarkable declaration that tells courts, investors, and tribunals that intra-EU claims under BITs or the ECT should not be considered and that awards should not be enforced. ⁵³

Table 5. EU states 2019 declaration against use or enforceability of intra-EU BITs and ECT

“1. Member States ‘by the present declaration... inform’ tribunals in all pending intra-EU BIT and ECT arbitrations about the legal consequences of Achmea as set out in the Declarations; and undertake, both as defending Member State and the claimant investor’s Member State, to inform tribunals of those consequences.
2. Defending Member States will request their national courts and any third country courts to set aside intra-EU BIT and ECT awards or not to enforce them due to a lack of consent to arbitration.
3. Member States “inform the investor community that no new intra-EU investment arbitration proceeding should be initiated”.
4. Member States which control organisations which have brought investment arbitration claims against another Member State will withdraw those claims.
5. Member States will terminate all intra-EU BITs by way of a plurilateral treaty or (if more expedient) bilaterally, ideally by 6 December 2019.
6. Settlements/awards in intra-EU BIT and ECT arbitrations which cannot be annulled or set aside and were voluntarily complied with or enforced before Achmea should not be challenged.”

This is a remarkable set of statements and actions by states which are party to BITs and the ECT, that they will request their courts not to enforce any awards made post-Achmea, and tell investors not to bring cases, and that these BITs will be terminated within less than a year. One legal commentator described this as ‘a comprehensive extermination’:

“it would appear that intra-EU investor-state arbitration is finally dead. By the Declarations, the Member States have fallen in line with the EC. The intention is to bring all existing intra-EU investor-state arbitrations to an end by the end of 2019, and prevent any new intra-EU arbitrations. By tackling not only the arbitrations but the treaties themselves, and “informing” tribunals and investors that arbitrations cannot be commenced or continue, Member States intend a comprehensive extermination of intra-EU arbitration.”⁵⁴

➤ **EU aims for global agreement, multilateral court, and revision of ECT**

On March 20, 2018, the Council of the European Union adopted negotiating directives authorizing the European Commission to negotiate a convention establishing a multilateral court for the

settlement of investment disputes (MIC).⁵⁵ However, these proposals only concern institutional issues, and do not provide for example rights for third parties to be represented, nor protection for democratic decisions, nor create any obligations on investors, leaving them in the privileged position of having only rights – unlike the CFIA proposals of Brazil, see above. (Hoffman 2018)

In June 2019 the EU Commission set out plans to renegotiate the terms of the ECT, including

“calling for the ECT to incorporate a ‘right to regulate’ provision, along with revising its existing terms on expropriation, which among other changes would be ‘appropriately defined to clarify the nature of indirect expropriation.’ [and] include provisions on sustainable development, including on climate change and clean energy transition”

The ECT conference itself in December 2018 acknowledged the need to revise the treaty to reflect changes in the energy sector and “updated standards related to investment protection”.⁵⁶

4.5 The erosion of ISDS from FTAs: removing, deferring, and allowing opt-outs

The ISDS provisions of FTAs, which provide the third main source of potential international investor claims, have come under considerable pressure in recent years from widely supported public campaigns. The proposed EU-USA trade agreement, known as TTIP, was effectively abandoned. Some new FTAs, such as CETA, include ISDS provisions, but others do not, including the USMCA, which replaced NAFTA, and the new EU-Mercosur agreement; others include significant exceptions, such as the TP-CTT for New Zealand, and the EU-Singapore for matters relating to Singapore’s water supply.

Table 6. Status of new FTA agreements and ISDS mechanisms 2019

Treaty		Status mid-2019	ISDS or MIC mechanism?	Exceptions?
USMCA	USA, Canada, Mexico	Signed	No	Transitional for Mexico
CETA	EU-Canada	Signed	MIC (but not yet in place)	Subject to each EU country ratifying
CPTPP	Canada-etc	Signed	ISDS	New Zealand can opt-out of ISDS
EU-Mercosur	EU, Mercosur		No	
EU-Singapore	EU, Singapore		ISDS	Singapore water supply
EU-Vietnam	EU, -Vietnam		MIC	
AfCFTA	African countries	Signed	No	-
RCEP	Southeast Asian countries	In negotiation	Reduced scope of ISDS	
TTIP	EU-USA	Abandoned	-	-

➤ New north American trade agreement USMCA scraps most ISDS

The United States Mexico Canada Agreement (USMCA), which has replaced NAFTA, has scrapped ISDS between Canada and the USA – while retaining some ISDS between Mexico and the others. The removal of ISDS provisions was strongly supported by USA legislators from both major parties: “in a

September 12, 2018 letter, 312 legislators—including Democrats as well as Republicans—from all 50 U.S. states wrote that they “strongly support” U.S. Trade Representative (USTR) Robert Lighthizer’s efforts to remove ISDS from NAFTA”⁵⁷

It was also strongly supported by long-standing social movement campaigns against ISDS in trade agreements: According to a leading Canadian campaigner:

“Under the USMCA, ISDS will be eliminated between Canada and the U.S., and scaled back between Mexico and the U.S. This is an incredible achievement. NAFTA’s ISDS mechanism, embedded in NAFTA Chapter 11, allowed investors to bypass the domestic courts and sue governments before private international tribunals when public policy choices, laws or regulations allegedly harmed their investments.... The fight against ISDS is far from over. But its phasing out between Canada and the U.S. and its retrenchment between Mexico and the U.S is a remarkable victory for social movements in North America and globally, who have tirelessly campaigned to eliminate this insidious impediment to progressive public policy.” (Sinclair 2018)

➤ **TTIP: dead**

Negotiations on TTIP, the proposed transatlantic FTA between the EU and the USA were effectively abandoned in 2016, though they have not been formally cancelled by either side. The campaigns on both sides of the Atlantic were the key factor in this. It also suits the protectionist rhetoric of President Trump, who strongly opposed and withdrew from TPP on the grounds of protecting USA sovereignty and business interests, but he has not yet denounced TTIP.

➤ **Transpacific trade agreement includes ISDS, but not signed by USA, exemptions for NZ**

The new *Comprehensive and Progressive Agreement for Trans-Pacific Partnership* (CPTPP) – involving most countries except the USA – does include ISDS provisions. But the USA has not signed this agreement. And the scope of ISDS was restricted: “side letters were also signed to exclude compulsory ISDS between New Zealand and five countries: Australia, Brunei Darussalam, Malaysia, Peru and Vietnam”.⁵⁸ The Australian Labor party agreed to CPTPP but promised that if it wins the next election it will “seek to remove ISDS provisions from existing free trade agreements and legislate so that a future Australian government cannot sign an agreement with such provisions.”⁵⁹

➤ **New EU-Mercosur trade agreement does not include investment chapter or ISDS**

In June 2019 the EU reached final agreement with Mercosur on a new free trade agreement. However, unlike the FTAs with Canada, Vietnam and Singapore “It does not include investment protection standards or dispute settlement on investment protection” , nor any provisions concerning expropriation.⁶⁰

➤ **Africa FTA signed but investment and ISDS provisions deferred**

The agreement establishing the African Continental Free Trade Area (AfCFTA) “entered into force on May 30, 2019, with the first phase of the deal taking effect for 24 countries. Phase II negotiations on intellectual property rights (IPRs), investment and competition policy are expected to take at least another year.” The provisions so far in place do not cover investment, expropriation or compensation⁶¹

➤ **RCEP: negotiations continue with reduced role for ISDS**

“After an RCEP negotiation round held in Singapore in late August 2018, most negotiating partners are reported to have agreed to reduce the scope of application of the ISDS clause. A senior official said that ISDS would not be applied on an MFN basis; accordingly, different RCEP members could agree to different dispute settlement regimes.”⁶²

5. Conclusion

5.1 Discussion

National law and practice on compensation provide political processes for resolving unusually direct and large conflicts between economic interest of the public and of investors. For the investors it is all about the final formulation determining the value of compensation, and the economic deterrent effect of this on policies which negatively affect investors' returns. But this is a perspective from one side only. For the public interest, it is about minimising the cost of policies which are valued as beneficial in themselves. This includes not only policies of extending public ownership to achieve economic reforms and social justice, but also the defence of other policies, such as the phasing-out of nuclear power, and generally the defence of democratic decision-making as a way of improving economic and social conditions, without being burdened by the economic penalty of indefinitely preserving investors' returns.

Firstly, the differences in the legal frameworks reveal the conflicts of interest underlying the issue. While the USA constitution gives a right to 'just compensation', interpreted as 'market value' by the courts, the national laws of the UK and Germany do not give investors any such simple right. The constitutional rules give quite different weights to conflicting interests, with Germany stating simply that compensation should reflect a balance of interest, the USA focussed entirely on investor rights, and the UK effectively allowing total discretion to the elected public authority of parliament.

Secondly, the national frameworks treat compensation as a political responsibility of public authorities. This is most obvious in the parliamentary autonomy of UK law, but is also visible in the reluctance of national courts in the USA and Germany to overrule judgments of public authorities on compensation unless these can be demonstrated to have been manifestly unreasonable. Under all these systems the decision-making process is political, which may be formalised through courts or administrative processes including the use of juries, and so subject to competing pressures from investors and public interest groups. It is the relative strength of these groups which determines the outcomes.

Thirdly, the methods for calculating compensation, even in the USA, are themselves part of the contestation process. There is no single formula used in negotiations under national laws, the texts of BITs and FTAS show significant variations in their wording on the 'value' of compensation, and even the basis of arbitration awards vary.

However, investors have frequently won compensation on terms which are much more favourable to them than to the public interest, frequently obtaining public finance to support continued enjoyment of previous returns. This unbalanced pattern undoubtedly reflects the general political dominance of commercial interests, but it is possible to identify a number of factors specific to the context of compensation for nationalisations.

Firstly, governments and public authorities have more complex political objectives, usually including the promotion of their country or region as business-friendly, both for national and international investors (this was an explicit objective even of the Chavez government in Venezuela). The payment of generous compensation is thus a tactic for reducing or avoiding conflict with investors over the public ownership policy, and over possible future investment in the economy, which reduces government incentive to protect public interest.

Secondly, the processes for determining compensation are often conducted through secret negotiations, or delegated to panels consisting of financial and legal advisors who are themselves part of the investor community. The opportunity for public debate is thus limited and as a result the expression of the public interest is weakened. This is also part of the attraction of arbitrations for investors, as tribunals members are nominated by parties and meet in secret, without allowing amicus curiae representations from NGOs. The secrecy of negotiations over FTAs or BITs has a similar advantage for investors. The outcome of the German court and parliamentary proceedings over the nuclear shutdown, which was conducted with great publicity and public interest and parliamentary debate, shows how a far more balanced result can be achieved in these conditions.

Thirdly, investors have by contrast simple objectives of maximising compensation and protecting future returns, minimising public ownership of profitable enterprises, and reducing the scope for political regulation of environmental impacts. They are thus prepared to use any tactics conducive to these aims, including the kind of unethical networking visible in the Baden-Wurtemberg case, or the creative accounting in the Missoula case in California.

In relation to the international agreements, however, we are now seeing a significant rebalancing of power towards the public interest. Proceedings against western European countries has provoked a public political backlash, reinforcing the public opposition to ISDS and rejecting the legitimacy of its use. The removal of ISDS from a number of recently negotiated FTAs – including NAFTA itself, the mother of such deals - and the uncertain future status of CETA, are one set of striking results of this public action, as a result of which the future use of such treaties to obtain compensation from high income countries must be in doubt. The increasingly strong action by the EU and member states against intra-EU BITs and the ECT are equally remarkable, leading to a confrontational standoff between arbitration tribunals on the one hand and the courts and institutions of the EU – and Germany – on the other hand. While this response is formally concerned with intra-EU action, it is hard to see western European countries being more relaxed if developing country investors bring cases against them. The termination of BITs by a number of developing countries shows the unwillingness of countries to continue accepting such intrusion on the sovereignty of their legal systems. The Calvo doctrine is quietly becoming the new global orthodoxy.

There are a number of factors that have contributed to this effective resistance to ISDS mechanisms. They include the widespread revival of nationalism, which includes a general resistance to international intrusion into national politics, and a re-assertion of national sovereignty. This is a factor in both developing countries, European countries, and the USA. This has formed an unlikely alliance against ISDS with the extensive public resistance to ISDS in its various forms, which is based on concern over democratic decision-making on a range of material issues, notably environmental issues of pollution and climate change, consumer protection and regulatory issues, and the development of public services, especially healthcare. The ECT cases, especially, have been directed at renewable energy policies and, in the case of Germany, anti-nuclear policy, which have been adopted as the result of strong public support and concern over climate change: “the mobilisation of European public opinion...[for] “a green, social, and humanitarian Europe” (Buonanno 2018).

Finally, a more general factor underlying the others is a resistance to the growth of corporate power which has been magnified and institutionalised by globalisation. This has been highly visible in organised form in the international campaigns against a range of trade and investor agreements, from the protests in Seattle and afterwards against the WTO trade rules and dispute mechanisms, through successive campaigns across many countries against proposed trade agreements including TTIP, CETA, and the trans-Pacific agreement. (Hopewell 2015, Hoekman and Kostecki 2009).

5.2 Principles for compensation for nationalisation

The following five principles are offered for determining compensation for nationalisation in a way which provides a fair balance between the private investors and the public interest. The first four principles are drawn from the conclusion to part 2 and the fifth is derived from the discussion of international investment law in sections 3 and 4. They relate to compensating shareholders for the nationalisation of companies – whether listed on the stock exchange or owned by private equity and other investors directly – including companies running PPPs.⁶³

A. Fairness to public interest

‘Compensation shall be determined by establishing an equitable balance between the public interest and the interests of those affected’.

The question of fair compensation for taking a company into public ownership involves fairness to two parties, and so the principle of balance should be central – as is expressed in the German constitution (2019).

A fair level of compensation must therefore take account not only of investors interests, but also the public interest, including the public interest in “measures of economic reform or measures designed to achieve greater social justice”⁶⁴ which, in the words of the UK courts, may require less than the ‘full market value’ which investors typically claim. Fairness to the public requires that the economic and social benefits of these reforms should be delivered and not negated by the cost of compensation.

Fairness to investors should involve returning to them the actual money which they have invested in the service. They should get their money back.

B. Returning shareholders’ actual investments

Compensation should do no more than return to the private shareholders the actual net assets in the company financed by shareholder equity. No compensation should be paid for loss of expected profits, nor for any value derived from government subsidy or support or regulatory regime, nor for any value derived from sale of assets or avoidance of pension liabilities or underperformance of statutory or regulatory duties or avoidance of tax.

The companies in parts of mature public service systems which have been privatised are not comparable to companies operating in other spheres. Their business is entirely framed by the requirements and licenses structured by the state and its democratic structures, which determine the public objectives of the system and its economic framework, including requirements such as universal service and the standards to be met. They have not built up the business through their own initiative, nor had to compete in a consumer market with other companies, and their investments are not made on the basis of entrepreneurial risk in consumer markets.

The income and returns of these companies reflect their success in obtaining concessions, contracts, or acquisition of state-owned enterprises, and interacting with regulators and politicians to maximise those returns. The regulatory system usually has the objective of ensuring that companies are sufficiently profitable for investments, and may be ‘captured’ by the private companies to permit higher levels of extraction. The actual returns of such companies are thus determined not by

successful market activity but by successful political activity in obtaining supportive terms from the state through its public service structure.

The renationalisation of privatised public service operators or the termination of public service concessions or contracts should not therefore require compensation as though the company had been built by private enterprise in a consumer market. It should simply reflect the principle that investors are entitled to get back the money they have actually invested in the companies. The core measure of this is the net assets in the company financed by shareholder equity as shown in the company books. The process of determining how much to return to shareholders should also take account of all relevant evidence including the extraction of value by various means, the extent to which shareholders' value has been based on state grants, their performance of their obligations, the financial responsibility of their management, reasonable expectation of risk management, and other factors.

The shareholders then get back all their actually invested net capital, and can invest it in any other enterprise of their choosing, without restriction.

C. No perpetuation of excessive or monopoly returns through 'market value'

Shareholders of companies brought into public ownership should not receive compensation which maintains for them the level of excessive or monopoly earnings or returns that they enjoyed during the period of privatisation.

The central objective of nationalisation or municipalisation of privatised utilities and other public services is to end the extraction of excessive returns by shareholders which are seen as excessive by public and their political representatives. Since these returns are typically extracted through monopolies or oligopolies or long-term low-risk concessions, it is economically more efficient to end such monopoly returns.

But the market value of companies is based on expected earnings, and enshrines the expectation of future continuation of those excessive and/or monopoly returns. The difference between the market value of a company and the book value of the actual shareholder investments in a company is, in accounting theory, determined by the extent to which the shareholders are enjoying 'abnormal returns' above the risk-free rate. (Feltham and Ohlson 1995). Paying market value as compensation thus defeats the main economic objective by enabling the private owners to continue to enjoy, even after nationalisation, the abnormal returns they had before nationalisation.

It would impose on consumers of the service (or tax-payers) the burden of paying, through a future publicly-owned company, charges which include the cost of financing the excessive returns to the private investors even after they have ceased to own or operate that company. This cost is in effect the same as the cost of the excessive extraction of profits under privatisation, so no economic benefit is gained by the public, and could remain a burden on the public for decades.

Paying compensation based on preserving into the future the current returns of the owners of the privatised companies, whether through using some measure of 'market value' or otherwise, is also economically inefficient. Firstly, it amounts to payment of a capitalisation of monopoly profits, and puts the investors into the privileged position of continuing to enjoy monopoly returns even after losing the monopoly itself. Secondly, in a globalised economy, any compensation paid may be invested or spent anywhere in the world, and so be lost to the national economy: compensation

should be minimised, rather than maximised. Thirdly, it eliminates the major efficiency saving of reducing the cost of capital under public ownership.

D. Public discussion and democratic processes

The process of determining actual compensation should be fully public including audits, hearings, and debates to ensure that the public interest can be heard and represented both by elected politicians and by civil society organisations.

Outcomes can be expected to reflect the relative strength of political and economic interests, but the chances of achieving a fair balance between the public interest and investors are greatly improved through public meetings, published audits, and full transparency including a role for civil society organisations.

E. Democratic public policy and national courts

Foreign investors should be “afforded no more than the same treatment as nationals” including “the right to file claims in the local judicial system”⁶⁵, but should not be able to obtain preferential treatment, or obtain decisions which frustrate a democratically determined policy, or overrule the decisions of national courts.

Compensation provisions in international treaties or agreements such as BITs should never be construed in such a way as to frustrate a democratic decision about the public interest and the structure of public service systems taken in accordance with national laws, nor to overrule the decisions of national courts. The public interest includes not only the benefits which are judged to flow from public ownership, but also the power of its elected representatives to decide what is in the public interest, especially in relation to public services, and the integrity of national legal systems and courts.

6. Annexes

6.1 BITs/ECT/FTAs definitions of compensation

Table 7. Definitions of 'value of investment' for compensation

Country	BIT/FTA with UK	Definition of value	
China	China BIT 1985 arts 5,7	Such compensation shall amount to the real value of the investment expropriated immediately before the expropriation or impending expropriation became public knowledge.	
Hong Kong	Hong Kong BIT arts 5, 8	Such compensation shall amount to the real value of the investment immediately before the deprivation or before the impending deprivation became public knowledge	
Malaysia BIT	Malaysia BIT arts 4,7	Such compensation shall amount to the value of the investment expropriated immediately before the expropriation or impending expropriation became public knowledge and shall be freely transferable. The legality of any such expropriation and the amount of compensation shall be determined by due process of law in the territory of the Contracting Party in which the investment has been expropriated.	
Singapore A	Singapore BIT 1975 arts 5, 8	Such compensation shall amount to the market value of the investment expropriated immediately before the expropriation or impending expropriation became public knowledge.	
Energy Charter Treaty (ECT)	ECT ; ECT (UNCTAD)	Such compensation shall amount to the fair market value of the Investment expropriated	
Singapore B 2018	EU-Singapore FTA 2018 nyr Arts 2, 3, 7	<p>Compensation shall amount to the fair market value of the covered investment immediately before its expropriation or impending expropriation became public knowledge Valuation criteria used to determine fair market value may include going concern value, asset value including the declared tax value of tangible property, and other criteria, as appropriate</p> <p>Art 3</p> <p><i>...(b) claims where a representative submits a claim in the name of a class composed of an undetermined number of unidentified claimants and intends to conduct the proceedings by representing the interests of such claimants and making all decisions relating to the conduct of the claim on their behalf shall not be admissible.</i></p>	

		... Article 2.3 (National Treatment) shall not apply to any measure relating to: (a) the supply of potable water in Singapore; (b) the ownership, purchase, development, management, maintenance, use, enjoyment, sale or other disposal of residential property or to any public housing scheme in Singapore.	
Canada	Canada-EU FTA (CETA) 2018 (investment chapter 8) nyr nif	The compensation referred to in paragraph 1 shall amount to the fair market value of the investment at the time immediately before the expropriation or the impending expropriation became known, whichever is earlier. Valuation criteria shall include going concern value, asset value including the declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.	

6.2 Cases under BITs, ECT, FTAs

Source: UNCTAD <https://investmentpolicy.unctad.org/investment-dispute-settlement>

<u>Name</u>	<u>Cases as Respondent State</u>	<u>Cases as Home State of claimant</u>
Argentina	<u>60</u>	<u>5</u>
Spain	<u>49</u>	<u>50</u>
Venezuela	<u>47</u>	<u>1</u>
Czechia	<u>38</u>	<u>5</u>
Egypt	<u>33</u>	<u>4</u>
Mexico	<u>30</u>	<u>4</u>
Poland	<u>30</u>	<u>7</u>
Canada	<u>28</u>	<u>49</u>
India	<u>24</u>	<u>6</u>
Russian Federation	<u>24</u>	<u>22</u>
Ecuador	<u>23</u>	0
Ukraine	<u>23</u>	<u>11</u>
Kazakhstan	<u>19</u>	<u>5</u>
Bolivia	<u>16</u>	<u>1</u>
Hungary	<u>16</u>	<u>1</u>
United States of America	<u>16</u>	<u>174</u>
Peru	<u>15</u>	<u>3</u>
Romania	<u>15</u>	<u>1</u>
Kyrgyzstan	<u>14</u>	0
Turkey	<u>14</u>	<u>33</u>
Slovakia	<u>13</u>	<u>1</u>
Turkmenistan	<u>13</u>	0
Croatia	<u>12</u>	<u>3</u>
Libya	<u>12</u>	0
Colombia	<u>11</u>	<u>1</u>
Italy	<u>11</u>	<u>37</u>

Moldova, Republic of	<u>11</u>	<u>1</u>
Bulgaria	<u>10</u>	0
Georgia	<u>10</u>	0
Algeria	<u>9</u>	0
Costa Rica	<u>9</u>	<u>1</u>
Jordan	<u>9</u>	<u>8</u>
Latvia	<u>9</u>	<u>3</u>
Pakistan	<u>9</u>	0
Serbia	<u>9</u>	0
Albania	<u>8</u>	0
Panama	<u>8</u>	<u>6</u>
Uzbekistan	<u>8</u>	<u>1</u>
Viet Nam	<u>8</u>	0
Indonesia	<u>7</u>	0
Korea, Republic of	<u>7</u>	<u>5</u>
Dominican Republic	<u>6</u>	0
Lithuania	<u>6</u>	<u>3</u>
Chile	<u>5</u>	<u>7</u>
Cyprus	<u>5</u>	<u>26</u>
Estonia	<u>5</u>	<u>2</u>
Guatemala	<u>5</u>	0
Lebanon	<u>5</u>	<u>3</u>
Mongolia	<u>5</u>	0
Montenegro	<u>5</u>	0
North Macedonia	<u>5</u>	0
Philippines	<u>5</u>	0
Saudi Arabia	<u>5</u>	<u>1</u>
Sri Lanka	<u>5</u>	0
Armenia	<u>4</u>	0
Bosnia and Herzegovina	<u>4</u>	0
Burundi	<u>4</u>	0
Congo, Democratic Republic of the	<u>4</u>	0
Greece	<u>4</u>	<u>14</u>
Kuwait	<u>4</u>	<u>7</u>
Laos	<u>4</u>	0
Madagascar	<u>4</u>	0
Morocco	<u>4</u>	0
Tanzania	<u>4</u>	0

Uruguay	<u>4</u>	0
Azerbaijan	<u>3</u>	0
Belarus	<u>3</u>	<u>1</u>
Belize	<u>3</u>	0
China	<u>3</u>	<u>5</u>
El Salvador	<u>3</u>	0
Germany	<u>3</u>	<u>62</u>
Malaysia	<u>3</u>	<u>4</u>
Mauritius	<u>3</u>	<u>8</u>
Oman	<u>3</u>	<u>2</u>
Paraguay	<u>3</u>	0
Senegal	<u>3</u>	0
Slovenia	<u>3</u>	<u>2</u>
United Arab Emirates	<u>3</u>	<u>10</u>
Yemen	<u>3</u>	0
Zimbabwe	<u>3</u>	0
Australia	<u>2</u>	<u>6</u>
Belgium	<u>2</u>	<u>18</u>
Ethiopia	<u>2</u>	0
Gabon	<u>2</u>	0
Gambia	<u>2</u>	0
Ghana	<u>2</u>	0
Honduras	<u>2</u>	0
Iraq	<u>2</u>	0
Lesotho	<u>2</u>	0
Mozambique	<u>2</u>	0
Nicaragua	<u>2</u>	0
Thailand	<u>2</u>	0
Austria	<u>1</u>	<u>22</u>
Bahrain	<u>1</u>	<u>1</u>
Bangladesh	<u>1</u>	0
Barbados	<u>1</u>	<u>6</u>
Benin	<u>1</u>	0
Cabo Verde	<u>1</u>	0
Cameroon	<u>1</u>	0
Equatorial Guinea	<u>1</u>	0
France	<u>1</u>	<u>49</u>
Grenada	<u>1</u>	0
Guyana	<u>1</u>	0
Iran	<u>1</u>	<u>2</u>
Kenya	<u>1</u>	0
Myanmar	<u>1</u>	0
Nigeria	<u>1</u>	0

Qatar	<u>1</u>	<u>4</u>
Rwanda	<u>1</u>	0
South Africa	<u>1</u>	<u>3</u>
Sudan	<u>1</u>	0
Syrian Arab Republic	<u>1</u>	0
Tajikistan	<u>1</u>	0
Trinidad and Tobago	<u>1</u>	0
Tunisia	<u>1</u>	<u>1</u>
Uganda	<u>1</u>	0
United Kingdom	<u>1</u>	<u>78</u>
Bahamas	0	<u>2</u>
Bermuda	0	<u>1</u>
British Virgin Islands	0	<u>1</u>
Denmark	0	<u>8</u>
Finland	0	<u>2</u>
Gibraltar	0	<u>2</u>
Hong Kong, China SAR	0	<u>1</u>
Ireland	0	<u>1</u>
Israel	0	<u>4</u>
Jamaica	0	<u>1</u>
Japan	0	<u>4</u>
Luxembourg	0	<u>40</u>
Macao, China SAR	0	<u>1</u>
Malta	0	<u>3</u>
Netherlands	0	<u>108</u>
Norway	0	<u>5</u>
Portugal	0	<u>5</u>
Seychelles	0	<u>1</u>
Singapore	0	<u>4</u>
Sweden	0	<u>10</u>
Switzerland	0	<u>32</u>

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8. Notes

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