RECENT INTERNATIONAL DECISION

INTERNATIONAL ARBITRATION — INVESTOR-STATE DISPUTE SETTLEMENT — TRIBUNAL HOLDS THAT URUGUAY'S ANTI-TOBACCO REGULATIONS DO NOT VIOLATE PHILIP MORRIS'S INVESTMENT RIGHTS. — *Philip Morris Brands Sàrl v. Oriental Republic of Uruguay*, ICSID Case No. ARB/10/7, Award (July 8, 2016).

Investor-state dispute settlement (ISDS) allows investors to sue states directly for violations of international investment agreements.[1] Over the past few decades, there has been a large increase in the number of such investment agreements[2] and ISDS provisions within them.[3] ISDS has been criticized as allowing corporate actors the power to chill government regulations via the threat of costly and prolonged litigation.[4] Recently, in *Philip Morris Brands Sàrl v. Oriental Republic of Uruguay*[5] (*Philip Morris v. Uruguay*), a tribunal of the International Centre for Settlement of Investment Disputes[6] (ICSID) found that two tobacco control measures adopted by Uruguay did not amount to an indirect expropriation of a tobacco company's investment nor to a denial of the company's right to fair and equal treatment under the Swiss-Uruguay Bilateral Investment Treaty[7] (BIT). Rather, it upheld Uruguay's sovereign power to regulate public health over Philip Morris's investment claims. The tribunal's decision to take a limited, pro-state approach to the claims asserted will prove to be a signal for potential future arbitration cases.

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[1] For an overview of the origins and development of ISDS, see Patricia Ranald, *Expropriating Public Health Policy: Tobacco Companies' Use of International Tribunals to Sue Governments over Public Health Regulation*, 73 J. AUSTL. POL. ECON. 76, 77–82 (2014).

[2] Benjamin Hawkins & Chris Holden, *A Corporate Veto on Health Policy? Global Constitutionalism and Investor-State Dispute Settlement*, 41 J. HEALTH POL. POL'Y & L. 969, 978 (2016). There are currently almost 3000 bilateral investment treaties and close to 400 other treaties with investment provisions. *See International Investment Agreements Navigator*, U.N. CONF. ON TRADE & DEV., http://investmentpolicyhub.unctad.org/IIA [https://perma.cc/H55G-EU97].

[3] Ranald, *supra* note 1, at 79.

[4] Hawkins & Holden, *supra* note 2, at 981–82; Ranald, *supra* note 1, at 84.

[5] ICSID Case No. ARB/10/7, Award (July 8, 2016), http://icsidfiles.worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C1000/DC9012_En.pdf [https://perma.cc/H5K2-EPW2].

[6] ICSID, established in 1966, is a global arbitration institute offering a forum for the resolution of international investment disputes. INT'L CTR. FOR SETTLEMENT OF INV. DISPUTES, ANNUAL REPORT 3, 11 (2016). As of 2016, there are 153 contracting states to the ICSID Convention, including the United States. *Id.* at 11. For background information on how ICSID operates, see generally *id.* at 26–29.

[7] Agreement Between the Swiss Confederation and the Oriental Republic of Uruguay on the Reciprocal Promotion and Protection of Investments, Switz.-Uru., Oct. 7, 1988, 1976 U.N.T.S. 389 [hereinafter BIT].

With "one of Latin America's highest rate of smokers,"[8] Uruguay must understandably be proactive in its tobacco-control regime. In 2008 and 2009, it enacted two public health measures restricting marketing of tobacco products.[9] The "Single Presentation Requirement"[10] (SPR) requires that cigarette brands sell only under a single package or variant.[11] The "80/80 Regulation"[12] mandates that the health warnings on cigarette packages increase from fifty to eighty percent of the surface of the packages.[13] Between 2010 and 2011, claims brought by subsidiaries of Philip Morris International regarding the SPR and 80/80 Regulation failed in several domestic challenges.[14] Subsequently, Philip Morris challenged these regulations as breaching Uruguay's obligations under several articles of the BIT.[15] In 2011, a three-person arbitration tribunal was convened under ICSID,[16] and two years later, the tribunal affirmed that it had jurisdiction over the challenge.[17]

The ICSID tribunal ruled against all of Philip Morris's claims. First, it examined the contention that the regulations expropriated Philip Morris's investment in its trademarks under Article 5(1) of the BIT, which prohibits states from taking measures that expropriate a corporation's investment, excepting certain circumstances for the public benefit with compensation for the investor.[18] Because the regulations did not interfere with Philip Morris's legal title to its investment, there was a potential case for only indirect, rather than direct, expro-

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[8] *Philip Morris*, Award, ¶ 75. In this context, Uruguay has been progressive in enacting a range of antismoking legislation. *Id.* ¶¶ 77–78. In 2003, it was the first Latin American state to sign the World Health Organization [WHO] Framework Convention on Tobacco Control, May 21, 2003, 2302 U.N.T.S. 166 [hereinafter WHO FCTC]. *Philip Morris*, Award, ¶¶ 85–86.

[9] *Philip Morris*, Award, ¶¶ 9–11. For an in-depth background on Uruguay's tobacco-control policies, see generally HOLLY JARMAN, THE POLITICS OF TRADE AND TOBACCO CONTROL 77–85 (2015).

[10] Ministerio de Salud Pública Ordenanza [Ministry of Public Health Ordinance] No. 514, de 18 de agosto de 2008 (Uru.).

[11] *Philip Morris*, Award, ¶ 10. Before 2009, Philip Morris's domestic subsidiary, Abal Hermanos, sold thirteen variants within six brand families. *Id.* ¶ 72.

[12] Ministerio de Salud Pública Ordenanza [Ministry of Public Health Ordinance] No. 466, de 1 de septiembre de 2009 (Uru.).

[13] *Philip Morris*, Award, ¶ 11.

[14] A challenge to the SPR was rejected by Uruguay's administrative law court in 2011, *id.* ¶ 158, and claims regarding the constitutionality of the law that delegated power for the enactment of the 80/80 Regulation failed in the Uruguay Supreme Court of Justice and administrative law court. *Id.* ¶¶ 166–167.

[15] *Id.* ¶ 12.

[16] *Id.* ¶ 19. Each party appointed one arbitrator; Philip Morris appointed Gary Born, an American national, and Uruguay appointed Professor James R. Crawford, an Australian national. *Id.* ¶ 18. As these two arbitrators could not agree upon a third member to serve as the president of the tribunal, ICSID's Secretary-General appointed Professor Piero Bernardini, an Italian national. *Id.*

[17] *Id.* ¶ 25.

[18] *Id.* ¶ 180; BIT, *supra* note 7, art. 5(1).

priation.[19] The standard for a finding of indirect expropriation used by the tribunal was a "substantial deprivation" of the value, use, or enjoyment of one's investment.[20] The tribunal stated that the 80/80 Regulation did not indirectly expropriate Philip Morris's investment because "distinctive elements" of the brand were still recognizable in the smaller allocated space on the packaging.[21] Neither did indirect expropriation result from the SPR, which did not cause a "substantial deprivation" of the value of Philip Morris's investments.[22]

In addition, though not necessary to the decision, the ICSID panel decided that Philip Morris's expropriation claims failed because the regulations were a valid exercise of Uruguay's police power, a principle embedded in customary international law.[23] The panel then provided a comprehensive history of the police power doctrine, from its beginnings in international law through its applications in previous arbitrations.[24] It drew upon this jurisprudence to find that the SPR and 80/80 Regulation, as actions "taken *bona fide* for the purpose of protecting the public welfare" that were "non-discriminatory and proportionate," satisfied the conditions for a state's exercise of regulatory powers not to constitute indirect expropriation.[25] The tribunal stated that protecting public health was "an essential manifestation" of the police power;[26] in doing so, it affirmed the power of a state's public health regulations over investors' claims.

The panel then addressed Philip Morris's claim that it was denied fair and equal treatment (FET) in violation of Article 3(2) of the BIT, which mandates "fair and equitable treatment" for investors.[27] The FET claim failed under the standard used by the tribunal. In finding the SPR not arbitrary, it focused on the fact that the measure was a good faith, reasonable "attempt to address a real public health con-

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[19] *Philip Morris*, Award, ¶ 191. Direct expropriation, no longer a major concern for investors, occurs when a state nationalizes, takes legal title of, or physically seizes private property. *See* Directorate for Fin. & Enter. Affairs, Org. for Econ. Co-operation & Dev. [OECD], *"Indirect Expropriation" and the "Right to Regulate" in International Investment Law* 2–3 (OECD Working Papers on Int'l Inv. No. 2004/04, 2004), http://dx.doi.org/10.1787/780155872321.

[20] *Philip Morris*, Award, ¶ 284.

[21] *Id.* ¶ 276.

[22] *Id.* ¶ 284.

[23] *Id.* ¶¶ 287, 300. The police power allows a state to take actions, for reasons of public security, health, and morality, that may cause economic damage to a private actor, without needing to compensate the private actor. *See id.* ¶ 291.

[24] *Id.* ¶¶ 287–307.

[25] *Id.* ¶ 305.

[26] *Id.* ¶ 291.

[27] BIT, *supra* note 7, art. 3(2). FET is grounded in the customary international law requirement of ensuring a minimum standard of treatment for another state's investors. *Philip Morris*, Award, ¶ 311. The exact determinants of FET have not been defined but depend on the context of a given case. *Id.* ¶ 320. For examples of principles relied upon by past tribunals, such as transparency, due process, and good faith, see *id.* ¶¶ 319–323.

cern."[28] Similarly, it stated that the 80/80 measure, also a "reasonable measure adopted in good faith," was not arbitrary;[29] additionally, "[s]ubstantial deference [was] due" to the national authorities' policy decision.[30] Furthermore, the regulations did not violate the investor's legitimate expectations because they neither exceeded a state's inherent power to regulate for the public interest nor modified the relied-upon regulatory framework "outside of the acceptable margin of change."[31]

The tribunal summarily disposed of the rest of Philip Morris's claims. Philip Morris's claim that Uruguay impaired the use and enjoyment of its investments was dismissed on similar grounds as the FET claim.[32] The company's claim that Uruguay breached commitments as to the use of trademarks failed after the tribunal concluded that trademarks were not "commitments" within the scope of the BIT.[33] Finally, the tribunal dismissed Philip Morris's denial of justice claims regarding allegedly contradictory domestic proceedings pertaining to the 80/80 Regulation because the procedural improprieties did not reach a high-enough threshold.[34]

Gary Born, Philip Morris's chosen arbitrator, wrote a concurring and dissenting opinion.[35] Though he agreed with most of the decision, he disagreed with two parts of its ruling on the FET claims.[36] First, he found that there had been a denial of justice in the domestic legal proceedings of Philip Morris's claims because of the contradictory treatment of certain aspects of the claims by Uruguay's Supreme Court and its administrative law court; this disparity was a breach of the FET guarantee of Article 3(2).[37] Second, he considered the SPR to be "arbitrary and unreasonable."[38] In his view, the SPR — an "internationally unique" requirement, with both "over-inclusive and under-inclusive" effects — did "not bear even a minimal relationship" with its

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[28] *Philip Morris*, Award, ¶ 409.

[29] *Id.* ¶ 420.

[30] *Id.* ¶ 418.

[31] *Id.* ¶ 423.

[32] *Id.* ¶¶ 444–446.

[33] *Id.* ¶ 482. "Commitments" was interpreted by the tribunal to mean a "specific obligation" undertaken by the state, *id.* ¶¶ 479–481, and trademarks were held to be part of a general legal framework rather than a specific promise made by the state, *id.* ¶ 481.

[34] *Id.* ¶¶ 576–580. Because a finding of denial of justice would essentially be "condemn[ing] the State's judicial system," *id.* ¶ 499, the tribunal held that there must have been an "*outrageous*" failure, rather than merely incompetent procedure, *id.* ¶ 500.

[35] *Philip Morris*, Award annex B (concurring and dissenting opinion by Gary Born).

[36] *Id.* ¶¶ 1–2.

[37] *Id.* ¶¶ 6–9. Uruguay's administrative law court (*Tribunal de lo Contencioso Administrativo*) and its Supreme Court had adopted differing interpretations on whether Uruguay's executive branch could require images covering more than fifty percent of a tobacco package. *Id.* ¶ 31.

[38] *Id.* ¶ 82.

cited objective.[39] However, he emphasized that he did not question Uruguay's authority to regulate public health and safety.[40]

The tribunal in *Philip Morris v. Uruguay* took a pro-state approach to the claims brought forward by the tobacco company, sending a signal for future antiregulatory litigation under investment treaties. Though the facts of the case highlighted certain systemic issues of ISDS, particularly the potential for corporate challenges to chill regulation, the tribunal limited the scope of the FET claims in a favorable manner for the state in two important ways. First, the tribunal recognized that Uruguay's status as a developing nation meant that Uruguay deserved particular deference to its policy decisions made with reference to international standards. Second, it reasoned that Philip Morris's legitimate expectations should have included increasingly stringent tobacco regulations. In doing so, the tribunal further empowered states to regulate dangerous consumer products such as tobacco. Though international arbitration opinions are not binding precedent, adjudicators do look to the core principles of past decisions for guidance.[41] Thus, the tribunal's approach in this case may disincentivize ISDS challenges, at least by tobacco companies in developing nations.[42]

This case illustrates some of the background controversies surrounding the ISDS system's potential to chill regulation. Some commentators believe that the nature of the investor-state dispute settlement system skews in favor of corporate actors because only corporations bring cases, whereas states are always defendants.[43] *Philip Morris v. Uruguay*, the first instance of a tobacco company di-

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[39] *Id.* ¶ 86. The dissent underscored the "limited documentary record" surrounding the adoption of the SPR as indicative of a lack of thorough deliberation. *Id.* ¶¶ 111–112.

[40] *Id.* ¶ 3; *see also id.* ¶ 197.

[41] JARMAN, *supra* note 9, at 21; *see also* Valentina S. Vadi, *Global Health Governance at a Crossroads: Trademark Protection v. Tobacco Control in International Investment Law*, 48 STAN. J. INT'L L. 93, 122–23 (2012) (describing the "path coherence" in such decisions).

[42] Professor Harold Koh, former Legal Adviser of the State Department, similarly argues that World Trade Organization (WTO) panels should take into account "human rights and public health considerations," and that such factors can be used as a "shield" to justify national regulations that might otherwise violate WTO regulations. Harold Hongju Koh, *Global Tobacco Control as a Health and Human Rights Imperative*, 57 HARV. INT'L L.J. 433 (2016).

[43] *See, e.g.*, Cecilia Olivet & Alberto Villareal, *Who Really Won the Legal Battle Between Philip Morris and Uruguay?*, THE GUARDIAN (July 28, 2016, 7:42 AM), https://www.theguardian.com/global-development/2016/jul/28/who-really-won-legal-battle-philip-morris-uruguay-cigarette-adverts [https://perma.cc/JSE4-4MC3]. Most disputes have been brought by investors from developed countries against developing countries. Ranald, *supra* note 1, at 82. Investors from developed countries have brought more than eighty percent of all claims, and in 2015, sixty percent of cases were brought against developing countries. U.N. Conference on Trade and Development, *Investor-State Dispute Settlement: Review of Developments in 2015*, at 3, U.N. Doc. UNCTAD/WEB/DIAE/PCB/2016/4 (June 8, 2016).

rectly suing a country in an international forum,[44] was the latest of a series of "industry-sponsored trade and investment challenges."[45] Even though the challenge failed and Philip Morris had to pay Uruguay $7 million and cover the fees for the tribunal,[46] Uruguay still had to expend significant resources, including financial costs of $2.6 million.[47] Thus, some commentators argue that states — especially developing nations — hesitate to enact regulations that may provoke a corporate challenge because of such financial burdens.[48] In fact, Uruguay itself was nearly pressured into relaxing the two measures underlying this litigation in 2010 after receiving initial notice of Philip Morris's claims.[49] Though the chilling effect is particularly potent for less developed nations,[50] threats of litigation from big tobacco have also chilled regulation in Canada, the European Union, and New Zealand.[51] However, despite these challenges for state actors, regulatory chill might subside in an arbitration climate that favors states over multinational corporations. Therefore, the pro-state manner in which this tribunal adjudicated the claims for both sides is a step toward ameliorating such regulatory chill in the future.

On the defendant side, the tribunal took into account Uruguay's "limited technical and economic resources,"[52] granting broad deference to the state's policy in response to Philip Morris's claim of arbitrari-

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[44] Benedict Mander, *Uruguay Defeats Philip Morris Test Case Lawsuit*, FIN. TIMES (July 8, 2016), https://www.ft.com/content/1ae33bc8-454e-11e6-9b66-0712b3873ae1 [https://perma.cc/G3DN-G4D3]. As Uruguay is a small market for tobacco product sales, with a total GDP of only $50 billion (USD), compared with Philip Morris's annual revenues of $80 billion, *id.*, some claim that this challenge was not about money but an opportunity for Philip Morris to test the potential for litigating regulatory measures under investment treaties. *See* JARMAN, *supra* note 9, at 81–82.

[45] Sarah A. Roache, Lawrence O. Gostin & Eduardo Bianco Fonsalia, *Trade, Investment, and Tobacco:* Philip Morris v Uruguay, 316 JAMA 2085, 2085 (2016). Philip Morris sued Norway in 2010 regarding its ban on displaying cigarettes in retail stores. *Id.* Philip Morris also helped fund a multicountry WTO challenge to Australia's plain packaging laws in 2014, though the WTO panel declined to exercise jurisdiction. Andrew Martin, *Philip Morris Leads Plain Packs Battle in Global Trade Arena*, BLOOMBERG (Aug. 22, 2013, 12:01 AM), https://www.bloomberg.com/news/articles/2013-08-22/philip-morris-leads-plain-packs-battle-in-global-trade-arena [https://perma.cc/5EVQ-PDSY]; *see also* Roache et al., *supra* (reporting on the case). For a history of tobacco litigation before international courts, see generally Sergio Puig, *Tobacco Litigation in International Courts*, 57 HARV. INT'L L.J. 383 (2016).

[46] *Philip Morris*, Award, ¶ 588.

[47] Olivet & Villareal, *supra* note 43. Former New York Mayor Michael Bloomberg helped fund Uruguay in this lawsuit. Mander, *supra* note 44.

[48] *See* Ranald, *supra* note 1, at 84. Though tobacco consumption has decreased in the United States and other developed countries, its use has increased in developing countries, partially as a result of free trade deals. Puig, *supra* note 45, at 388–89.

[49] *Uruguay to Relax Tobacco Laws to Combat Philip Morris Claim*, GLOBAL ARB. REV. (July 28, 2010), http://globalarbitrationreview.com/article/1029479/uruguay-to-relax-tobacco-laws-to-combat-philip-morris-claim [https://perma.cc/3ZMY-VZYG].

[50] Vadi, *supra* note 41, at 97.

[51] JARMAN, *supra* note 9, at 3.

[52] *Philip Morris*, Award, ¶ 393.

ness.[53] It found, as the plaintiffs alleged, that the SPR had not been subject to detailed research prior to its enactment.[54] However, it was enough that Uruguay had adopted such measures in conformity with the World Health Organization's guidelines;[55] there was no need for additional evidence to support its regulations.[56] Indeed, the tribunal ruled that what mattered was not whether the regulations actually had the intended effects, or if the impacts of the regulations could even be measured,[57] but whether they were "reasonable" when adopted.[58] And it was reasonable for Uruguay, a developing nation, to rely upon international guidelines in creating policies.[59] The deference shown by the tribunal, insofar as it influences future panels, may thus reassure developing countries. Though they may not have the resources to thoroughly test and measure each regulation, they may still be able to go ahead and regulate as long as they follow authoritative international frameworks.

Second, on the plaintiff side, the tribunal narrowly defined the scope of Philip Morris's legitimate expectations within the FET claim.[60] Tribunals have been willing to protect investors' expectations of a stable regulatory framework;[61] however, the requirement of legitimate expectations does not limit a state's right to regulate.[62] Legitimate expectations, rather, hinge upon "*specific* undertakings" made by the state,[63] and states retain flexibility to adapt regulations to changing circumstances.[64] Past cases developed this idea by requiring investors

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[53] *Id.* ¶¶ 393–396; *see also* Koh, *supra* note 42, at 446.

[54] *Philip Morris*, Award, ¶ 407.

[55] Uruguay enacted its regulations following guidelines of the WHO FCTC, *supra* note 8. *Philip Morris*, Award, ¶ 360. The WHO FCTC aims "to protect present and future generations from the devastating . . . consequences of tobacco [use] . . . by providing a framework for tobacco control measures." WHO FCTC, *supra* note 8, art. 3. The tribunal recognized that these guidelines in fact were specifically implemented to support nations with resource constraints. *Philip Morris*, Award, ¶¶ 91, 396.

[56] *Philip Morris*, Award, ¶¶ 394–396.

[57] *Id.* ¶ 306.

[58] *Id.* ¶¶ 409, 417.

[59] *Id.* ¶¶ 393–394, 396; *see also International Tribunal Upholds States' Rights to Protect Health Through Tobacco Control*, WHO (July 12, 2016), http://www.who.int/fctc/mediacentre/news/2016/international-tribunal-states-rights-to-protect-health-through-t/en/ [https://perma.cc/8S7Q-E72B] (noting the tribunal's favorable reception of an amicus brief explicating the WHO's expertise on matters of public health).

[60] For a history of the legitimate expectations doctrine, see Michele Potestà, *Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept*, 28 ICSID REV. FOREIGN INV. L.J. 88, 98–121 (2013).

[61] *Id.* at 111.

[62] *Philip Morris*, Award, ¶ 422.

[63] *Id.* ¶ 426.

[64] Potestà, *supra* note 60, at 112–13, 117.

to take a holistic account of the state's regulatory environment.[65] *Philip Morris v. Uruguay* extended this line of thought by curbing an investor's expectations based on a specific harmful product, tobacco, and its unique local and global regulatory environment.[66] In particular, it decided that cigarette manufacturers cannot expect to avoid "onerous" regulations;[67] in fact, they should only expect "progressively more stringent regulation."[68] Given the "widely accepted articulations of international concern for . . . tobacco [use]," even the novelty of the regulations at hand did not violate Philip Morris's legitimate expectations.[69] In essence, the decision placed the onus on Philip Morris to anticipate and adapt to regulatory measures.

In granting substantial deference to policy decisions in light of Uruguay's economic circumstances and in narrowly defining the legitimate expectations of tobacco companies, *Philip Morris v. Uruguay* established solid guidance for future challenges by tobacco companies to public health regulations under international investment treaties. The decision has particular impact given the current ISDS system in which investor challenges are most commonly levied against developing countries. Professor Harold Koh takes the more confident view that this case is "an unequivocal landmark rebuke" of big tobacco's trade arguments.[70] Thus, this decision may strengthen states' confidence in enacting tough and innovative tobacco control measures. Other states may take even bigger steps. India, for instance, has proposed to entirely ban foreign investment from big tobacco.[71] Here, a similar battle is gearing up — Philip Morris has raised issues of India's compliance under various trade treaties.[72] Though it is doubtful that we have seen the last of tobacco plaintiffs in ISDS, the decision in *Philip Morris v. Uruguay* should certainly give big tobacco plaintiffs pause.

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[65] *Id.* at 118. Factors for holistic consideration have included political, cultural, and economic circumstances. *Id.*; *see also* Methanex Corp. v. United States, Final Award, Part IV, Ch. D, ¶¶ 9–10 (Aug. 3, 2005), 16 ICSID Rep. 32 (2012) (finding that Methanex should have expected to be subjected to California's "vigilant" regulatory environment); Biwater Gauff (Tanz.) Ltd. v. United Republic of Tanz., ICSID Case No. ARB/05/22, Award, ¶ 376 (July 24, 2008), http://icsidfiles.worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C67/DC1589_En.pdf [https://perma.cc/7SCB-7NMF] (stating that investors should be aware that investment climates in developing countries may not be easy).

[66] Koh, *supra* note 42, at 446–47.

[67] *Philip Morris*, Award, ¶ 429.

[68] *Id.* ¶ 430.

[69] *Id.*

[70] Koh, *supra* note 42, at 447. Koh argues that tobacco control should be the "number one human rights and public health imperative" in trade law. *Id.* at 434.

[71] *Philip Morris Jolted by Indian Proposal to Ban Foreign Tobacco Investment*, CNBC (Jan. 16, 2017, 1:41 AM), http://www.cnbc.com/2017/01/16/philip-morris-jolted-by-indian-proposal-to-ban-foreign-tobacco-investment.html [https://perma.cc/NU7Z-US3C].

[72] *Id.*