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Using investor-state dispute settlement to enforce investor obligations

by

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International investment agreements (IIAs) are generally one-way instruments: they establish obligations for host countries only. These obligations can be far-reaching in their implications, often affecting core government functions. They are enforced through strong investor-state dispute-resolution mechanisms (ISDS). Thus, IIAs can considerably limit host countries' regulatory powers, without imposing substantive responsibilities on foreign investors. At best, IIAs condition the exercise of certain rights by foreign investors upon compliance with national law (through so-called "legality" or "compliance" clauses).

IIA provisions, not least those defining protected investments, have allowed a remarkable expansion of potential beneficiaries of rights over the same investment. Several related entities forming a corporate chain may be entitled to bring claims, even for the same loss. And, in addition to the absence of investor obligations in IIAs, these treaties do not make such related entities liable for any illegality committed in relation to an investment. Except when any of the foreign entities is a party to the investment instruments, as a general matter only the local company may be held liable for illegalities committed in a host country's territory. Further, host countries generally will not be able to use the dispute-resolution mechanism in IIAs against such local companies or indeed even against protected investors.

In the case of shareholder claims, investment tribunals consider that shareholders hold a protected investment under IIAs. This investment consists of a direct or indirect shareholding in a company constituted in the host country (and sometimes also other interests in that local company). According to investment tribunals, shareholders can bring claims against any measure "affecting" their investments. However, foreign shareholders are generally neither parties to the contracts concluded by the local company nor subject to local regulations. Therefore, they are deemed not bound by obligations applicable to the local contracting company. The upshot is that, on the one hand, IIAs entitle foreign shareholders to bring claims in respect of measures taken against the local company and its assets. On the other hand, as to the local company's obligations, the "corporate veil" limiting the company shareholders' liability tends to be strictly observed.

Further, one of the most important concepts of international investment law is the distinction between claims whose "fundamental basis" is a contract, which are subject to the contract and to national law, and claims whose "fundamental basis" is a treaty, which in principle are subject to international law. Thus, "whether there has been a breach of the [investment treaty] and whether there has been a breach of contract are different questions" in the eyes of an investment tribunal.[1] Jurisdictional and merits defenses based upon contractual or national law provisions *vis-à-vis* treaty claims are generally disregarded.[2] Also, to the extent jurisdiction is founded on the "treaty" basis of a claim, counterclaims by the host country invoking contractual or national law provisions have been considered inadmissible.[3]

IIA negotiators could consider providing for the right of the respondent government to:

- Invoke, as defenses against treaty claims, breaches of obligations related to an investment deriving from any legal source, even if the claimant itself is not bound by these obligations as a matter of contract or national law.
- Bring counterclaims against treaty claims based upon the breach of contractual or national law obligations applicable to the investment (i.e., the local company), even if the claimant itself is not bound by these obligations as a matter of contract or national law.[4]

Challenges to the legitimacy of the investment-protection regime are manifold. Still, making investment arbitration work to protect the rights of (at least) both parties to the investment relationship seems like one of the obvious places to start to boost the regime's legitimacy. If IIAs and investment tribunals are allegedly more adequate to deal with foreign investment issues than national institutions, why should they not be equally open to both investors and host countries?

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[1] *Compañía de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic*, ICSID Case No. ARB/97/3, Decision on Annulment (July 3, 2002), para. 96.

[2] Recently, however, the concept of "admissibility" has been applied to reject part of a treaty claim on the basis of a contractual provision. *See Hochtief AG v. Argentine Republic*, ICSID Case No. ARB/07/31, Decision on Liability (December 29, 2014), paras. 187-194.

[3] This does not mean that counterclaims are not possible under existing IIAs; they require however certain interpretations that investment tribunals should but have so far not generally adopted.

[4] The role under IIAs of contract and national law obligations directly applicable to an investment should be considered separately from "public interest" issues under international law, such as human rights and the

protection of the environment. The scope of the obligations is different, although some overlaps exist. Further, the instruments and institutions dealing with the two kinds of obligations are often national in respect of the first category and international as to the second. Yet, expanding the role of IIAs in fostering respect for these international public interest issues should also form part of the agenda for reform of international investment law.

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