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Can host countries have legitimate expectations?

by

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The concept of “legitimate expectations” was introduced into the legal relations between foreign investors and host country governments to denote that the latter cannot act contrary to certain expectations they have set in the past. Absent a clear-cut framework regarding which expectations qualify as “legitimate”, dispute-settlement practice indicates that such expectations can be relevant under fair-and-equitable treatment and indirect expropriation articles in international investment agreements (IIAs). They can be based on:

- Governments’ written commitments to investors, e.g., contractual commitments beyond mere contractual expectations;
- Governments’ representations vis-à-vis *specific* investments, e.g., direct and public endorsements; or
- Host countries’ unilateral representations, e.g., favorable regulatory frameworks as they existed at the time of an investment.¹

Foreign investors can claim breach when host countries fail to fulfill expectations based on any of these sources. Since the early 2000s, “legitimate expectations” have often been invoked in investor-state arbitrations.

By analogy, the question arises whether host countries too can have legitimate expectations concerning the behavior of foreign investors within their economies, absent any specific investor obligations in IIAs. Such expectations could be inferred from treaty preambles recognizing the objectives of IIA parties’ economic or “sustainable development”, as well as articles providing that investors “shall strive to carry out the highest level possible of contributions to the sustainable development of the host State and the local community”² or corporate social responsibility (CSR) articles reaffirming “the importance of each Party encouraging enterprises ... to voluntarily incorporate into their internal policies those internationally recognised standards, guidelines and principles of [CSR]”.³ Expectations could be based on:

- Investors’ written commitments to host country governments, e.g., contractual infrastructure commitments concerning the quality of services such as water and sanitation;⁴
- Investors’ representations, e.g., statements by corporate executives about contributions their investments will make to a host country; or
- Investors’ unilateral representations, e.g., as evidenced by CSR policies or by support for such instruments as the United Nations (UN) Guiding Principles on Business and Human Rights, the UN Global Compact or the OECD Guidelines for Multinational Enterprises.⁵

Host countries could claim breach when investors fail to fulfill expectations based on any of these sources.

In any event, assessing the legitimacy of expectations involves an inherent, context-bound balancing of investors’ and states’ expectations. Arguably, in fact, even the assessment of investor’ legitimate expectations under the current approach should require that a state’s legitimate expectations are taken into account.

Countries are beginning to refer to their own expectations. In *Sempra v. Argentina*, for example, Argentina argued that it “had many expectations in respect of the investment that were not met or otherwise frustrated ... [such as] that the investor would bear any losses resulting from its activity, work diligently and in good faith, not claim extraordinary earnings exceeding by far fair and reasonable tariffs, resort to local courts for dispute settlement, dutifully observe contract commitments, and respect the regulatory framework” in response to the investor’s claim that its expectations went unfulfilled.⁶ While the expectations of Argentina did not play a significant role in the outcome of this particular case, Argentina’s reference to such expectations *per se* illustrates their inherent relevance to disputes between investors and host countries.

However, since governments currently cannot initiate IIA-based arbitral proceedings against foreign investors, their reliance on legitimate expectations is limited to counterclaims brought in response to investors’ claims.⁷

Tentative steps are underway toward reducing this asymmetry and laying the ground for recognizing host countries’ legitimate expectations. For example, more than 75% of IIAs concluded between 2008 and 2013 reference “sustainable development” or “responsible business conduct”.⁸ Future IIAs could explicitly stipulate that host countries’ legitimate expectations are protected (or, going further, recognize investor obligations) and establish an independent, substantive right to claim for breach of host countries’ legitimate expectations, provided that treaty-based or domestic regulatory prerequisites regarding consent are satisfied. This would help to ensure that IIAs further the interests of all parties and, in so doing, contribute to a more balanced international investment regime—thereby strengthening the regime’s legitimacy.

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¹ Christoph Schreuer and Ursula Kriebaum, “At what time must legitimate expectations exist?,” in Jacques Werner and Arif Hyder Ali, eds., *Law Beyond Conventional Thought* (London: Cameron May, 2009), pp. 265-276.

² Brazil–Mozambique CIFA, art. 10, available at <http://www.iisd.org/sites/default/files/publications/comparison-cooperation-investment-facilitation-agreements.pdf>.

³ Trans-Pacific Partnership (2016), art. 9.17.

⁴ See, e.g., *Biwater Gauff (Tanzania) Ltd. v. Tanzania*, ICSID Case No. ARB/05/22, Award (Jul. 24, 2008), paras. 381-382.

⁵ See, e.g., BASF, “Our responsibility to respect human rights,” available at <https://www.basf.com/en/company/sustainability/employees-and-society/human-rights.html>.

⁶ *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Award (Sept. 28, 2007), para. 289.

⁷ While “contributory fault” may curb host countries’ responsibilities insofar as claimants’ actions contribute to the outcome that prompted claims, this principle does not create obligations for investors nor result in direct responsibility. See, *Yukos Universal Limited v. Russia*, PCA Case No. AA 227, Final Award (Jul. 18, 2014), pp. 500-510.

⁸ Kathryn Gordon, Joachim Pohl and Marie Bouchard, “Investment treaty law, sustainable development and responsible business conduct: a fact finding survey,” available at <http://dx.doi.org/10.1787/5jz0xvvgx1zlt-en>, pp. 10-11.

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