Kluwer Arbitration Blog

International Arbitration as the New Frontier for Reconceptualizing the International Legal Personality and Responsibility of Foreign Investors in the Post-Pandemic World

Mevelyn Ong (Sullivan & Cromwell) · Monday, December 12th, 2022

The author presented on this topic at the ACICA/CIArb Future Frontiers Conference, held in Melbourne, Australia on 7 November 2022 during Australian Arbitration Week. This piece elaborates on the presentation that was delivered.

In the last decade, as more states have refused to comply with arbitral awards, attempts have been made to seize the assets of state-owned entities in satisfaction of states' arbitral debts. Underlying many of these cases is a reconceptualization of the international legal personality of the state, and of its corresponding rights, immunities and obligations. Flowing from the introduction of the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles for Business and Human Rights, we have also seen the emergence of a similar conversation regarding the international legal personality and responsibility of non-state actors, specifically of foreign investors.

The post-pandemic era has further fueled, and amplified, this reconceptualization of the international legal personality and responsibility of foreign investors – through the avalanche of ESG regulations worldwide mandating human rights due diligence reporting across global supply chain networks, the proliferation of sanctions levelled against businesses and financial institutions involved in or facilitating transnational crime such as modern slavery or money laundering, the intensified policy initiatives promoting transitions to greener economies, and also, the promulgation of new generation treaties expressly imposing sustainable development obligations on foreign investors.

Against this backdrop, the traditional Westphalian state-centric conceptualization of international law is being increasingly challenged, the once-disparate fields of public international law and investment law are converging, and the question being increasingly asked is not what rights a foreign investor has, but rather, what obligations a foreign investor owes instead. It becomes worthwhile then to take a step back and consider whether the international arbitration community is prepared for this new post-pandemic era focused on advancing sustainable development. In re-examining the status quo, this piece will analyze three pre-pandemic arbitral cases. These three cases stand out for their particular prescience and together exemplify how international arbitration is becoming the new frontier through which foreign investors may be recognized as subjects under

international law, and consequently have responsibilities, if not obligations, vis-à-vis international human rights, the environment, and good governance.

I. Recognizing Foreign Investors as Subjects Under International Law

The first case is *Urbaser* v. *Argentina* (ICSID Case No. ARB/07/26), where the tribunal recognized that because "international law accepts corporate social responsibility as a standard of crucial importance for companies operating in the field of international commerce," "it can no longer be admitted that companies operating internationally are immune from becoming subjects of international law." The tribunal considered that whereas "positive" international law obligations "to perform" could only bind states, "negative" obligations – *i.e.* directions to respect a particular right, and not "engage in activity aimed at destroying" such rights – could be of "immediate application, not only upon States, but *equally* to individuals and other private parties." (Emphasis added; Paras 1195, 1199, 1208-1210).

Second, in *Bear Creek* v. *Peru* (ICSID Case No. ARB/14/21), the tribunal did not adopt *Urbaser*'s distinction between "positive" or "negative" international law obligations. Instead, the tribunal was divided on whether a particular international instrument – there, the International Labour Organization's Indigenous and Tribal Peoples Convention (ILO Convention 169) – imposed "direct" obligations on non-state actors. Whereas the majority decided that the Convention imposed "direct obligations on states only," the dissenting arbitrator opined that "does *not*…mean that [the Convention] is without significance or legal *effects*" for a foreign investor. (Emphasis added). In recognizing that "indigenous and tribal peoples also have rights under international law and these are *not* lesser rights" subordinated to an investor's rights, the dissenting arbitrator found that an investor's international law "responsibilities are no less than those of the government." (Emphasis added). In the dissenter's view, a "significant and material" failure to comply with such responsibilities led to damages being halved. (Dissenting opinion, paras 9-10, 36-39).

Finally, in *David Aven* v. *Costa Rica* (Case No. UNCT/15/3/, para. 738), the tribunal went further than both *Urbaser* and *Bear Creek*, finding that international law obligations that could be characterized as "obligations *erga omnes*" – such as those concerning the "protection of the environment" – could be imposed on foreign investors because in falling within the "concern of all states," states would have a "legal interest in their *protection*." (Emphasis added, para 738). *David Aven* thus opened the door to the possibility of foreign investors being not only obliged to *respect* certain international law rights (*i.e. Urbaser*'s so-called "negative" obligations), but being additionally obliged to proactively *protect* such rights (*i.e.* "positive" obligations).

When viewed together, the *Urbaser*, *Bear Creek* and *David Aven* trio reflect changing understandings of the international legal personality of foreign investors. Concerns as to whether such a conceptual evolution is contentious can be addressed by recalling that investment treaties governing the relationship between state and foreign investor are typically interpreted pursuant to the *Vienna Convention on the Law of Treaties (VCLT)*, and accordingly, ought to be interpreted in light of the treaty's object and purpose, and keeping in mind any relevant rules or principles of international law such as (but not limited to) "respect for, and observance of, human rights." Recognizing that foreign investors can be subjects of international law and have associated responsibilities, if not obligations, under international law thus becomes not so much an exercise of mental gymnastics, but rather an exercise of purposive and contextual interpretation, one that

recognizes that investment law and international arbitration should not operate in a silo carved out from the broader auspices of international law and international law developments. *See further e.g.*, here (para 1189 and 1200) and here.

II. The International Law Responsibility of Foreign Investors

Intertwined with the emerging recognition of the foreign investor as subjects of international law is the idea that responsibility for respecting and protecting human rights, preserving the environment, and not undermining good governance, is and should be a joint responsibility for *both* state and investor. Perhaps the more critical, and controversial, issue then is how the international responsibility of the foreign investor can be accounted for.

In *Bear Creek* – the only case of the trio of cases discussed herein that endeavoured to give force to this idea [1)] – the tribunal accounted for the joint responsibility of the state and the investor as a question of damages. For the majority of the tribunal, joint responsibility was accounted for by quantifying the impact of the state's action on the economic viability of the underlying investment, and considering the investor's non-compliance with international law only to the extent that such non-compliance had an economic impact on the investment's future profitability. Not only did this focus leave the impact of non-compliance on the local indigenous community out of the calculation (and therefore unremediated), but it turned a blind eye to the counterfactual impact of what would have happened to the broader human rights or environmental landscape had there been no state action taken, *i.e.* the non-economic impacts. The *Bear Creek* dissenter's alternative focus on quantifying the investor's "contribution to the events" that led to the state's action was equally problematic to the notion of joint responsibility, albeit for a different reason – such an approach runs the risk that an investor can choose to not comply with international human rights or environmental law safe in the knowledge that such non-compliance will merely be considered a form of contributory negligence that will offset or discount part of the damages award, but will not otherwise deprive him of compensation. Neither approach to accounting for the joint responsibility of the state and the investor for international human rights and the environment seems satisfactory. In fact, both approaches seem disconnected and at odds with a rapidly-changing world where the spotlight is increasingly on investors to assess, report and address human rights and environmental impacts in their operations or along their supply chain, and where states have made greater commitments to uphold human rights or taken bolder action to transition to greener economies. *See further* here and here.

Instead of accounting for the joint responsibility of the state and the investor as a question of damages, perhaps more thought ought to be given to recognizing that responsibility as a question of admissibility or of jurisdiction. *See further e.g.*, here, here, and here. There are cases, for example, where tribunals have invoked an international public policy against corruption as a jurisdictional or admissibility bar, or have recognized that investment protection ought not to be granted at the outset for investments "made in violation of the most fundamental rules of protection of human rights." As to whether an international public policy yet exists recognizing corporate social responsibility – specifically, an investor's responsibility (if not obligation) towards international human rights and the environment (as opposed to only vis-à-vis corruption) – it is worth noting that the tribunal in *Urbaser* v. *Argentina* opined that "international law accepts corporate social responsibility as a standard of crucial importance for companies operating in the field of international commerce." The unanimous adoption by the *Bear Creek* tribunal of the

"social license to operate" concept – a term used to define the "broader scope" of the responsibility of companies to respect human rights – should also not be overlooked. Although it remains to be seen whether future tribunals will solidify this notion further, recognizing the existence of such an international public policy could assist in accounting for the joint responsibility of the state and the investor for international human rights and the environment, while being a less controversial alternative than attempting to identify and inflict specific "hard" international law obligations not otherwise imposed on investors by international law itself.

III. Looking Forward

Overall, the *Urbaser*, *Bear Creek* and *David Aven* trio reflects an evolving understanding of the international legal personality and responsibility of non-state actors, specifically foreign investors. In the post-pandemic world, the foreign investor will not only have to be cognizant of an increasing array of obligations with an ESG flavour arising under the domestic laws of the countries in which it operates, but also of responsibilities, if not obligations, arising under international law as well. Not only will disputes regarding the substance and scope of such international law responsibilities and the consequences of non-compliance be increasingly encountered in the international arbitration arena, but the way such disputes are resolved will also force us as international arbitration practitioners to consider what role we want to play in a post-pandemic world more focused on advancing sustainable development globally.

References

?1 This is likely because in both *Urbaser* and *David Aven*, the invocation of the international law obligation was defeated (or perhaps more precisely, left unresolved as *obiter* statements) at the merits stage of the proceedings, and that being so, the tribunal in both *Urbaser* and *David Aven* did not have the opportunity to consider how to account for the joint responsibility of the state and investor. Both tribunals similarly considered that the international law obligations respectively invoked by the respondent states in their counterclaims were not "based on international law" per se, but rather as arising in relation to the underlying investment treaty. *See, Urbaser* v. *Argentina*, at para 1206-1209; *David Aven* v. *Costa Rica*, at para 739-743. This dichotomy seems odd, considering that in order to succeed in raising the counterclaim in the first instance (an endeavour in which they did succeed, as both tribunals accepted jurisdiction), the respondent states needed to establish a sufficient nexus to the investor's claim which arose from the underlying investment treaty. By contrast, in *Bear Creek*, the international law obligation invoked – being, whether the claimant investor had obtained a "social license" in accordance with ILO 69 – was a crucial issue accounted for at the damages assessment point instead; *Bear Creek Final Award*, at para 408.

This entry was posted on Monday, December 12th, 2022 at 8:19 am and is filed under foreign direct investment, Foreign Dispute, Foreign Investment Law, ISDS, ISDS Reform
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.