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Has ISDS Become a Tool for Promoting Business Sustainability?

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Investor-State dispute settlement (ISDS) has been widely criticized for being a tool in the hands of multinational companies, used to challenge domestic public policy measures even when legitimately adopted in the public interest. Critiques have been notable concerning the asymmetrical nature of international investment agreements (IIAs). While IIAs were concluded to afford protection to foreign investors against host States' abuses, thereby encouraging foreign investments, it is a fact that IIAs have not been traditionally conceived to hold investors internationally accountable for social or environmental damage caused in the course of their activities.

Yet, recent ISDS decisions and newly concluded IIAs are increasingly supportive of business sustainability. Recent literature further seem to put faith in the ability of ISDS to ensure compliance with principles of corporate social responsibility (CSR). This blog post explores ISDS's potential to endorse and promote business sustainability within the limits of the existing system and the challenges posed to its ongoing reform.

Business Responsibilities under International Law

Intergovernmental organizations have been at the forefront of promoting responsible business conduct, originally through soft law norms. These include norms focusing on specific areas of CSR, such as the United Nations Guiding Principles on Business and Human Rights *(UNGPs), the* International Labour Organisation's Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy*, or the* standards published by the International Organization for Standardization (ISO). International Standard ISO 26000, for instance, addresses social responsibilities that are relevant to an organization's mission and vision, while the ISO 14000 family of standards provides practical tools for enterprises to manage their environmental responsibilities. Other norms such as the OECD Guidelines for Multinational Enterprises, cover broad areas of CSR including human rights, social rights, or environmental protection.

Often used by brands as part of their marketing strategies, international guidelines and standards may incentivize businesses to adopt more sustainable conduct. However, because they are not binding, the ability of soft law norms to address violations of CSR-related standards at the international level is rather limited. Further, while investors can be bound by certain obligations contained in international treaties and instruments concluded by States, the application of such principles has been restrained outside the domestic arena by the absence of specific international *fora* for their implementation.

The Role of ISDS Tribunals in Applying CSR Principles

In the context of this legal vacuum, tribunals resolving investment disputes may increasingly become relevant to ensuring investor compliance with social responsibility principles. This section focuses on key CSR-related findings which could set the ground for the promotion of responsible investment through ISDS.

One important doctrine relevant to the enforcement of CSR standards is the 'clean hands' doctrine, albeit not approached homogeneously by ISDS tribunals. Some tribunals have declined jurisdiction to hear claims related to foreign investors' acts of fraud, bribery, or money laundering, or rejected the admissibility of such claims (e.g., *World Duty Free v Kenya*, *Metal-Tech v Uzbekistan*, *Niko Resources v Bangladesh*). Other tribunals have refused to consider these types of issues at the jurisdiction or admissibility stage, preferring to address claimants' alleged violations at the merit or quantum stages. For example, in the *Yukos* and related cases, the tribunals took into account the claimants' tax avoidance in their analyses of contributory fault, by agreeing to a 25 percent reduction of the damages awarded.

In the last decade, arbitral tribunals have tended to broaden the scope of their findings on CSR violations. In *Copper Mesa v Ecuador, the tribunal, following a line of arbitral decisions on contributory fault*, assessed for the first time the contribution of the foreign investor's human rights violations to its own losses. The tribunal determined that the claimant had initiated a 'reckless escalation of violence' (para 4.265), thus contributing to the loss of its investment in Ecuador and, therefore, reduced the damages awarded to the investor by 30 per cent (para 6.133).

Furthermore, arbitral tribunals have considered CSR obligations in their decisions on counterclaims for social or environmental damage raised by States against foreign investors. Although rarely successful in practice — damages were awarded based on counterclaims in only two publicly known cases: *Burlington Resources Inc v Ecuador*, and *Perenco Ecuador Ltd v Ecuador and Empresa Estatal Petroleos del Ecuador* — tribunals have shown an increased willingness to admit such claims within the limitations imposed by the underlying IIAs or contracts, and the procedural rules applicable to the cases in question.

Several reasons explain the limited incidence and success of counterclaims in investor-State arbitration proceedings. First, most IIAs do not expressly provide for the possibility of claims being brought by States, and some expressly limit claims to those from investors (e.g. article 26(2) of the Energy Charter Treaty (1998) or article XII(3) of the Canada-Venezuela BIT). Often, the underlying IIA neither expressly authorizes nor excludes counterclaims. In this case, the host State has to prove either the existence of a separate agreement to arbitrate counterclaims (see *Burlington* case), or an implied consent to counterclaims (see *Goetz v Burundi*, *Al Warraq v Indonesia*, *Urbaser v Argentina* and *Aven v Costa Rica*), for a treaty-based tribunal to establish its jurisdiction over a counterclaim. In addition, counterclaims have to meet admissibility requirements, which include requirements that they be closely related to the investment and the claimant's claim (e.g. *Al Warraq v Indonesia*) and that the host State itself, rather than third parties, was damaged as a result of the harm caused by the foreign investor (e.g. *Chevron v Ecuador II*). Finally, counterclaims shall be based on the violation of either an international obligation directly applicable to the investor, or an international or domestic obligation applicable under the underlying IIA. In the *Burlington* and *Perenco cases*, for instance, both tribunals awarded damages to Ecuador resulting from the investors' violations of Ecuador's domestic environmental law, which was applicable under article 42(1) of the ICSID Convention.

The Development of More Balanced Approaches in New Generation IIAs

The decisions issued by ISDS tribunals likely have inspired a new generation of IIAs increasingly including standards applicable to foreign investors. However, reform efforts have been too slow and fragmented to mark a significant evolution of the ISDS system.

A number of multilateral and bilateral instruments have reaffirmed the host State's right to regulate in the public interest and included 'soft' standards in their preambles or in discrete provisions. For instance, in the CETA's Preamble, enterprises operating within the territory of the Parties or subject to their jurisdiction, are encouraged "respect internationally recognised guidelines and principles of corporate social responsibility, including the OECD Guidelines for Multinational Enterprises, and to pursue best practices of responsible business conduct". More rarely, treaties impose binding obligations on foreign investors.

At the regional level, African States have been particularly innovative in creating investor obligations for CSR. The Economic Community of Western African States (ECOWAS) Supplementary Act on Investments, for instance, requires that investors refrain from corrupt practices (article 13), respect and uphold human rights principles (article 14), and comply with standards of corporate governance (article 15) and CSR (article 16). Other multilateral initiatives have led to the adoption of model instruments imposing CSR obligations that should serve in future negotiations of IIAs. Thus, the Pan-African Investment Code (PAIC) provides *inter alia* that investors shall meet accepted standards of corporate governance (article 19), refrain from corruption (article 21), contribute to the economic, social and environmental progress of the host State (article 22.3) and comply with business ethics and human rights (article 24).

The new Africa Arbitration Academy (AAA)'s Model BIT for African States goes even further in its definitions of foreign investors' obligations. These include obligations to respect the principles of human dignity and equality including in their dealings with indigenous people (article 1), to comply with environmental and social assessment processes in the host State (article 9), to respect labour and human rights obligations and promote gender equality (article 10), to abstain from corruption, money laundering and terrorism financing (article 12), to ensure that investments meet or exceed accepted standards of corporate governance (article 13), and to adopt high degrees of socially responsible practices in accordance with the OECD Guidelines for Multinational Enterprises (article 18). All these instruments allow for counterclaims (article 18, ECOWAS Agreement; article 43, PAIC; article 22 G., AAA's Model BIT).

At the bilateral level, the Morocco-Nigeria BIT, marks an interesting development in the history of investment treaties, by specifically providing for obligations relating to the respect of human rights, environmental, labour, anti-corruption and CSR standards (articles 13 to 19). The treaty notably provides for the mandatory completion of impact assessments (article 14) and requires certain companies to maintain a certification to ISO 140001 or equivalent environmental management standard (article 18). Other recent BITs require that investors "strive to achieve the highest possible level of contribution to the sustainable development" of the host State and engage in responsible business conduct (article 9, Brazil-Malawi BIT; article 14, Brazil-Ethiopia BIT).

From the Promotion of Foreign Investments to the Promotion of Responsible Foreign Investments

The ability of ISDS to promote sustainable business is naturally limited as it generally relies on foreign investors' prerogative to initiate proceedings against host States. However, recent decisions of arbitral tribunals and the new generation IIAs tend to limit investors' prospects of success if they have not complied with sustainable principles of business conduct.

If ISDS practice continues to evolve in this direction, foreign investors may be both encouraged to respect corporate responsibility norms and dissuaded from bringing claims against host States if they have failed to follow such norms. ISDS would thus still serve its original purpose of promoting foreign investments, with the caveat that it would only promote investments that conform to basic principles of business sustainability.

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