Briefing

Law

Keywords:
International investment, foreign investment, international law, investment treaties, human rights, legal tools

iied

Durham University

Issue date
February 2019

Policy pointers

Disputes between investors and states can affect third parties, including local residents and indigenous peoples. Yet these actors have little or no voice in investor-state dispute settlement (ISDS) proceedings, which can undermine their rights.

The ongoing UNCITRAL process is an opportunity for states to reform ISDS. But meaningful change requires addressing fundamental asymmetries in the system, including how to strengthen third-party rights.

Possible reform options include requiring that investors exhaust domestic remedies before accessing ISDS, so third parties can intervene in national proceedings, and creating a legal right for directly affected third parties to intervene in ISDS, to protect their rights and enforce relevant investor obligations.

The immediate challenge is for the relevant UNCITRAL working group to inscribe the issue in its reform agenda – understanding that any solutions will require careful thought and consideration.

Reforming investor-state dispute settlement: what about third-party rights?

The international investment regime is facing sustained calls for reform. Most debate centres on disputes between investors and states. But foreign investment projects can also affect third parties — including local residents and indigenous peoples. Existing arrangements for third parties to participate in investor-state dispute settlement (ISDS) are not designed to protect people whose rights and interests are directly at stake. This can undermine their rights and the ability of tribunals to consider all relevant facts and laws. A working group of the United Nations Commission on International Trade Law (UNCITRAL) is now considering reforming ISDS. Meaningful reform requires addressing fundamental asymmetries in the international investment regime and exploring how to strengthen the procedural rights of third parties. This policy brief discusses the issues and outlines possible ways forward.

The case for reform

Foreign investors use broad substantive protections granted by international investment treaties to challenge wide-ranging measures host states may have taken to advance public policy goals. Concerns about the balance between corporate and public interests have been magnified by the fact that arbitral tribunals — usually comprised of three private individuals — are called to review the conduct of governments, legislatures or domestic courts based on treaty standards that leave significant scope for discretion.

One problem is that the international investment regime is asymmetrical. Usually investors alone can initiate investor-state arbitrations under investment treaties primarily aimed at protecting their assets. A few respondent states have brought counterclaims against the investors that initiated the proceedings, asking the tribunal to examine whether alleged investor misconduct caused social or environmental harm. But counterclaims rarely succeed and raise questions about how payments can be used to provide redress to those most directly affected.

Similarly, a few recent investment treaties (or treaty templates) require investors to comply with international instruments — for instance on labour, environmental protection or human rights.[1] States could invoke such clauses in investor-state dispute settlement (ISDS). But treaty practice is yet to consolidate. And the clauses are less likely to make a difference if the people affected by their violation have no means to enforce them.

As investor-state claims increase, public scrutiny has intensified — leading commentators to talk of

a 'legitimacy crisis'.[2,3] And in the past, sustainable development was rarely considered in how investment treaties were interpreted and applied. Now, new international instruments, including the Sustainable Development Goals (SDGs, Box 1), mean that states and other relevant actors should ensure coherence between investment policies and social and environmental commitments.

Contemporary investment disputes are complex — often rooted, at least in part, in disputes involving people affected by the investment

Investment should not be an end in itself, but a means to an end: mobilising assets and capabilities to realise the SDGs.[4] This strengthens the case for redressing asymmetries and ensuring that investments advance sustainable development.

The UNCITRAL Working Group: an opportunity for real reform?

As part of wider efforts to reform the international investment regime, UNCITRAL Working Group III on ISDS Reform provides a multilateral forum for states to explore and possibly negotiate the reform of ISDS.[5] As UNCITRAL is part of the United Nations, realising the SDGs should be at the centre of its work.

The Working Group has interpreted its mandate as being limited to procedural dimensions. This restricts scope for discussion. But effective procedural reforms could help address some aspects of the system's asymmetries. In November 2018, the Working Group concluded that it is desirable to reform three aspects of ISDS: i) consistency, coherence, predictability and 'correctness' of arbitral decisions; ii) independence, impartiality, diversity and other concerns about arbitrators; and iii) cost and duration of investor-state claims.

These issues are important and potentially far reaching. But they do not constitute a comprehensive reform agenda. More fundamental questions need answering about the international investment regime, including ISDS. Does it promote investment that advances the SDGs? Do its benefits outweigh its costs? Could alternative policies be more effective?[7]

The Working Group is yet to fully discuss the asymmetrical nature of ISDS. Under which circumstances can investors bring claims? For example, any new multilateral ISDS-related treaty might require that investors can only access ISDS if they comply with national law and international standards of responsible investment. Also, should rules enable states to hold investors to account for alleged violations of their obligations? And how can third-party rights be protected in the proceedings?[8,9]

How the rights of third parties are at stake

The place of affected third parties in the international investment regime has received limited attention and is worth exploring more fully. Most debate about ISDS reform focuses on disputes between investors and states. But many large-scale projects also involve a wider web of relations. Contemporary foreign investment disputes are complex — often rooted, at least in part, in disputes involving people affected by the investment.[10]

Take the case of extractive industry projects. These can have profound impacts on indigenous peoples and local communities whose social identity, way of life and livelihoods are tied to land and natural resources. Projects can affect their rights, expropriate their land, pollute their water, fell their forests or change migration flows into the area.

From these people's viewpoint, the investor and the state work closely together. The government may have offered incentives, facilitated consultations and helped establish the project. Sometimes, state agencies have a stake. When this occurs, affected people may have few choices but to mobilise, protest or litigate against the investor and/or the state to enforce their rights or resist the project.

This is reflected in the reality of many investor-state arbitrations.[11,12] Several cases begin when state agencies — prompted by third-party action — review their position and take measures that adversely affect the investment. Foreign investors may respond by initiating ISDS proceedings — or accuse the state of failing to adequately respond to local actions, for example by protecting the investor's assets against damage or occupations (see Figure 1).

Box 1. The Sustainable Development Goals

In September 2015, the UN General Assembly adopted a plan of action containing 17 SDGs, accompanied by 169 more specific targets and a comprehensive set of indicators to measure progress.[6] The SDGs aim to guide the global agenda for 2015–2030. They range from ending poverty to combating climate change and promoting access to justice.

SDG 17 recognises the relevance of a global partnership to realise the SDGs and calls for enhancing policy coherence for sustainable development. This reinforces the need for states to establish effective rules, institutions and processes to ensure that business activity is aligned with the SDGs and contributes to achieving them.

In such cases, the interests of third parties may be at stake in the investor-state arbitration. Proceedings may also affect their legal rights in domestic or international human rights law. Foreign investors can protect their rights through ISDS. But affected third parties may face legal and practical barriers in accessing recourse under international human rights law or advancing their rights or interests in investor-initiated ISDS proceedings.

One problem is that the remit of ISDS tribunals is usually limited to the relevant investment treaty. Often, these instruments do not affirm the rights of affected people — although the applicable international rules require tribunals to take account of any other relevant, applicable norms, including domestic and human rights law, when interpreting investment treaties and settling disputes.[13,14]

Even the few recent investment treaties that explicitly require investors to both comply with domestic law and uphold international standards of responsible business conduct, for example on human rights, labour or the environment, do not consistently spell out the implications of these provisions in a dispute settlement context. Workers or local residents may be most directly affected by investor non-compliance, and could play an important role in holding investors to account for violations. But this is not yet part of the international investment regime.

Taken together, these circumstances raise questions. How effective is the international investment regime in grappling with the complexities of contemporary investment disputes? This relates to substantive rights and obligations established in the treaties, but procedural aspects are also relevant.

Why current procedures are inadequate

Investment relations involve multiple actors with different — and often competing — rights and obligations. Most legal systems have substantive and procedural rules to address this type of complexity: for instance, courts have arrangements to consider the views, rights and obligations of actors who are not a party to a dispute.[15] But ISDS lacks comparable mechanisms.

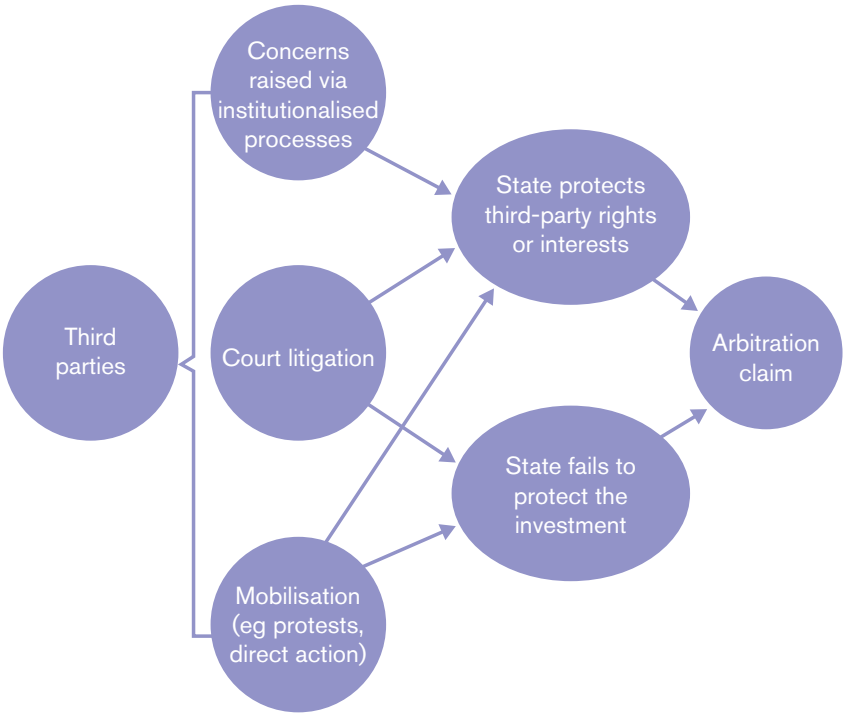
Depending on applicable rules, third parties may be allowed to provide input in the form of *amicus curiae* ('friends of the court') submissions. But these are subject to the tribunal's discretion and arbitration rules do not ensure third parties' access to hearings or documents submitted by the parties. Also, *amicus curiae* submissions mainly provide the tribunal with relevant information on points of fact or law. They are not designed to grant effective voice or protection for actors whose rights or interests are directly at stake in a dispute.

Likewise, a government should represent the interests of rightsholders within its jurisdiction in any dispute with the investor. But this cannot be assumed in practice. There may be tensions and even litigation between authorities and communities. And a government may not wish to highlight possible human rights failures of an investor that might expose its own.

This lack of effective arrangements for third-party participation in ISDS can undermine their rights or interests, and closes a possible route to hold investors to account for non-compliance with their obligations. It can also hamper how ISDS tribunals consider different perspectives on the facts or relevant applicable norms, including domestic and human rights law.[16] If third parties cannot independently voice their concerns in investment disputes this can erode the quality of decisions and the legitimacy of the system.

This runs counter to the aims of the SDGs, including ensuring 'equal access to justice for all' (SDG 16.3), developing 'effective, accountable and transparent institutions at all levels' (SDG 16.6) and ensuring 'responsive, inclusive, participatory and representative decision making at all levels' (SDG 16.7).

Figure 1. Third party rights in the factual fabric of ISDS disputes



Source: adapted from Cotula and Schröder (2017), based on a review of 20 ISDS cases.

The need for systemic reform

Addressing these issues requires comprehensive reform of the international investment regime — starting by clearly identifying its fundamental problems and reforming wider domestic and international legal frameworks.

Where problems are rooted in domestic legal systems, national law reform could strengthen the substantive and procedural rights of those affected. This could include better local consultation and public participation in investment approval processes — providing a framework for investors, public authorities and affected people to discuss and cooperate before and after investment decisions, to prevent rather than quell disputes.[17]

If domestic mechanisms fail, international human rights law should provide the main arena for affected people to pursue international redress. It contains relevant norms and its recourse institutions are specialists in handling human rights issues. The ongoing negotiation of a proposed binding treaty on business and human rights could transform this area of international law.[18]

In this wider reform context, effective ISDS reforms could help ensure the rights and interests of third parties are properly considered in settling investment disputes.

The UNCITRAL process: possible reform options

The Working Group could address some of these concerns. Possible reform options include requiring that investors exhaust domestic remedies before accessing ISDS, so third parties can intervene in national proceedings, and creating a legal right for directly affected third parties to intervene in ISDS, to protect their rights throughout the proceedings and enforce relevant investor obligations.[19]

Exploring these options will raise difficult issues. Tribunals may lack the appropriate expertise to adjudicate disputes where third-party rights — and possibly human rights — are at stake. Local communities may find themselves in an unfavourable dispute settlement forum: far from their locality, expensive and specialising in legal arrangements which protect foreign investors. How can they represent themselves and participate in ISDS? How can they be sheltered from risks associated with legal proceedings? And how would the system intersect with domestic and international human rights litigation?

But in the short term, the challenge for the Working Group is to consider the issue and to inscribe it in the reform agenda — while understanding that any reform will require careful thought and consideration.

Lorenzo Cotula and Nicolás M Perrone

Lorenzo Cotula is a principal researcher in law and sustainable development in IIED's Natural Resources Group. Nicolás M Perrone is an assistant professor of international law at Durham Law School.

Thanks to Alessandra Arcuri, Brooke Güven, Terrence Neal and David Schneiderman for their comments, though the views and any errors are the authors'.

Notes

[1] Examples include the Belarus-India BIT 2018 (Article 11i), the Intra-MERCOSUR Investment Facilitation Protocol 2017 (Article 13), and the Morocco-Nigeria BIT 2016 (Article 18). None of these treaties is yet in force. See also the Netherlands Model Investment Treaty 2018 (Article 7(1)). / [2] See for example Kelsey, J (9 January 2018) The crisis of legitimacy in international investment agreements and investor-state dispute settlement. ISDS Platform. https://isds.bilaterals.org/?the-crisis-of-legitimacy-in / [3] See also Arcuri, A (2019) The great asymmetry and the rule of law in international investment arbitration. In: L Sachs*et al.* (eds). Yearbook on international investment law and policy 2018, Oxford University Press. / [4] See also UNCTAD, UNCTAD's Reform Package for the International Investment Regime, Geneva, UNCTAD, https://investmentpolicyhub.unctad.org/Upload/Documents/Reform_Package_web.pdf / [5] UNCITRAL, Working Group III, 2017 to present: Investor-State Dispute Settlement Reform, http://bit.ly/2HWBUVZ / [6] Transforming our world: the 2030 Agenda for Sustainable Development, A/RES/70/1 (21 October 2015). https://sustainabledevelopment.un.org/post2015/transformingourworld / [7] Johnson, L, Skartvedt Güven, B, and Coleman, J (11 December 2017) Investor-State Dispute Settlement: What Are We Trying to Achieve? Does ISDS Get us There? CCSI blog. https://bit.ly/2M88UsE / [8] Cotula, L and Güven, B (7 December 2018) Investor-state arbitration: an opportunity for real reform? IIED blog. http://bit.ly/2SfDuXX / [9] See also Dietrich Brauch, M (21 December 2018) Multilateral ISDS Reform is Desirable: what happened at the UNCITRAL meeting in Vienna and how to prepare for April 2019 in New York, IISD blog. https://bit.ly/2WZbXZD / [10] Perrone, NM (2016) The international investment regime and local populations: are the weakest voices unheard? *Transnational Legal Theory* 7(3): 383–405. / [11] Perrone, NM (2019) The "invisible" local communities: foreign investor obligations, inclusiveness and the international investment regime. *American Journal of International Law Unbound* 113: 16–21. / [12] Cotula, L and Schröder, M (2017) Community perspectives in investor-state arbitration. IIED, London. http://pubs.iied.org/12603IIED. / [13] Article 31(3)(c) of the 1969 Vienna Convention on the Law of Treaties. / [14] Article 42(1) of the 1965 Convention on the Settlement of Investment Disputes Between States and Nationals of Other States. / [15] Examples of diverse legal configurations include Articles 64–77 of Germany's Federal Code of Civil Procedure; Rule 8A of Order I, First Schedule of India's Code of Civil Procedure; Articles 119–124 of Brazil's Code of Civil Procedure; and Rules 18–20 and 24 of the United States Federal Rules of Civil Procedure. International law examples concerning disputes between states include Article 62 of the Statute of the International Court of Justice; Article 31 of the Statute of the International Tribunal for the Law of the Sea; and Article 10 of the World Trade Organization's Dispute Settlement Understanding. / [16] Columbia Center on Sustainable Investment and UN Working Group on Business and Human Rights (2018) Impacts of the international investment regime on access to justice: roundtable outcome document. http://bit.ly/2GuTnTj / [17] Nicolás M. Perrone (2019) Making Local Communities Visible: A way to prevent the potentially tragic consequences of foreign investment?. In: Trubek, D, Thomas, C and Alvaro Santos (eds) G*lobalization Reimagined: A Progressive Agenda for World Trade and Investment Law*. Anthem. / [18] OHCHR, Open-ended intergovernmental working group on transnational corporations and other business enterprises with respect to human rights. www.ohchr.org/en/hrbodies/hrc/wgtranscorp/pages/igwgontnc.aspx / [19] International human rights norms and institutions, including in the context of ongoing discussions about a proposed treaty on business and human rights, would be the more appropriate place for rightsholders to initiate free-standing claims against states or investors.

Contact
Lorenzo Cotula
lorenzo.cotula@iied.org

80–86 Gray's Inn Road
London, WC1X 8NH
United Kingdom

Tel: +44 (0)20 3463 7399
www.iied.org

IIED welcomes feedback via: @IIED and www.facebook.com/theiied

ISBN 978-1-78431-663-1

This briefing has been produced with the generous support of Danida (Denmark), Irish Aid and Sida (Sweden). However, the views expressed do not necessarily represent those of the institutions involved.

Ministry of Foreign Affairs of Denmark
Danida

Irish Aid
Rialtas na hÉireann
Government of Ireland

Sida