



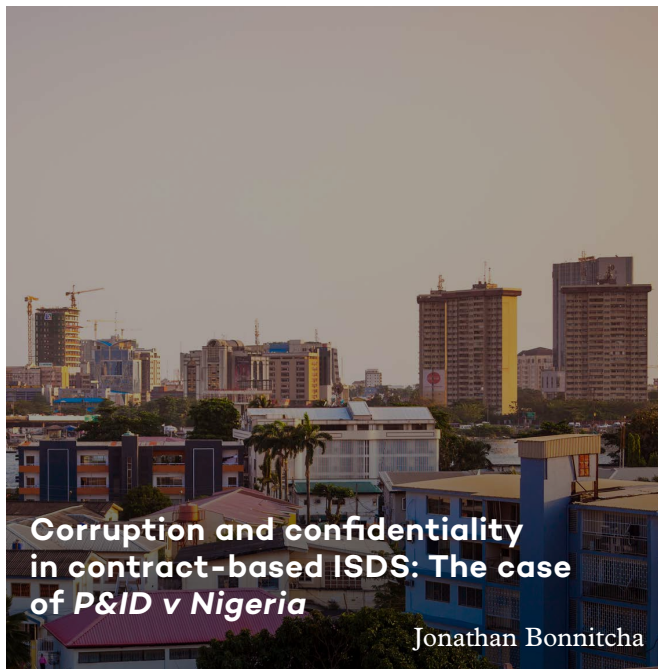
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Rethinking investment law from the ground up: extractivism, human rights, and investment treaties

Lorenzo Cotula



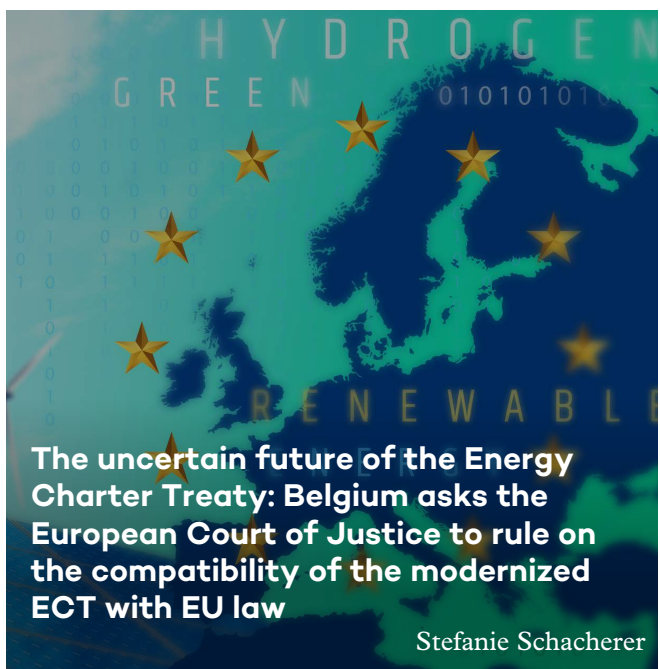
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LIST OF ACRONYMS

ASEAN	Association of Southeast Asian Nations
BIT	Bilateral Investment Treaty
CETA	Comprehensive Economic and Trade Agreement
CJEU	Court of Justice of the European Union
COMESA	Common Market for Eastern and Southern Africa
CPTPP	Comprehensive and Progressive Trans-Pacific Partnership
CSR	Corporate Social Responsibility
EAC	East African Community
EC	European Commission
ECJ	European Court of Justice
ECOWAS	Economic Community of West African States
ECT	Energy Charter Treaty
EU	European Union
FDI	Foreign Direct Investment
FET	Fair and Equitable Treatment
FTA	Free Trade Agreement
GATT	General Agreement on Tariffs and Trade
ICC	International Chamber of Commerce
ICS	Investment Court System
ICSID	International Centre for Settlement of Investment Disputes
ICSID Convention	Convention on the Settlement of Investment Disputes between States and Nationals of Other States
IIA	International Investment Agreements
IISD	International Institute for Sustainable Development
ILO	International Labour Organization
ISDS	Investor–State Dispute Settlement
ITN	Investment Treaty News
MFN	Most-Favoured Nation
MIC	Multilateral Investment Court
NAFTA	North American Free Trade Agreement
OECD	Organisation for Economic Co-operation and Development
PCA	Permanent Court of Arbitration
PPP	Public–Private Partnership
RCEP	Regional Comprehensive Economic Partnership
SADC	Southern African Development Community
SCC	Stockholm Chamber of Commerce
SDG	Sustainable Development Goal
TFEU	Treaty on the Functioning of the European Union
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
USMCA	United States–Mexico–Canada Agreement
VCLT	Vienna Convention on the Law of Treaties
WTO	World Trade Organization



INSIGHT 1

Rethinking investment law from the ground up: extractivism, human rights, and investment treaties

Lorenzo Cotula



Efforts to reform the investment treaty regime have gained traction but are narrowly conceived, as if the treaties existed in isolation from wider governance frameworks.¹ Specialization pushes lawyers toward circumscribed remits, while prevailing investment policy narratives focus on investor–state relations and macro-level issues such as cross-border investment flows. Renewed interest in how the treaties interact with other international norms, including on human rights,² has yet to translate into substantial investment treaty reconfigurations.

Such trends contrast with the local realities of investment relations. Though the state plays a central role in investment regulation and approval, large-scale projects often involve or affect broader constellations of actors,

each with different and possibly competing interests. Also, the application of investment treaties typically intersects with other rules of national and international law, and a treaty’s practical implications partly depend on these rules. Governance arrangements raise difficult questions about reconciling commercial interests with economic development, social justice, and environmental protection. And while investor–state dispute settlement focuses on reparations the state may owe to the investor, proceedings can have wider governance ramifications, affecting actors and rights beyond the conventional investor–state dyad.³

Large-scale investments in the natural resource sector illustrate these complexities. Mining, petroleum, logging, and agribusiness operations can have far-reaching impacts on small-scale farmers, forest dwellers, pastoralists, and artisanal fishers, including groups that international law recognizes as Indigenous Peoples. Relations between companies, affected people, and the different branches of government often engage diverse legal instruments that underpin conflicting claims—from constitutional provisions and sectoral legislation to international treaties protecting foreign investment, human rights, or the environment. Further, the approach a government takes to natural resource development may diverge significantly from what local groups advocate for. Thus when, for example, a state defends itself in investor–state arbitration, it does not necessarily protect the same interests as local groups.

In these respects, extractive industry investments can expose systemic tensions permeating the governance of foreign investment. Exploring how investment treaties operate in these settings can reshape how we

¹ This article largely summarizes a longer piece: Cotula, L. (2020). (Dis) integration in global resource governance: Extractivism, human rights, and investment treaties. *Journal of International Economic Law* 23(2), 431–454, <https://academic.oup.com/jiel/article/doi/10.1093/jiel/jgaa003/5875706>. The longer article provides more comprehensive references to support the points made. I am grateful to Jesse Coleman, Nicolás Perrone and Zoe Phillips Williams for comments on the ITN piece.

² The United Nations Working Group on Business and Human Rights has convened a consultation on these issues: <https://www.ohchr.org/EN/Issues/Business/Pages/IAs.aspx>. See also the open letter by several United Nations human rights mandate holders in connection with the work of the United Nations Commission on International Trade Law (UNCITRAL)’s Working Group III on Investor-State Dispute Settlement Reform (7 March 2019), https://uncitral.un.org/sites/uncitral.un.org/files/public_-_ol_arm_07.03.19_1.2019_0.pdf.

³ See also Perrone, N.M. (2016). The international investment regime and local populations: Are the weakest voices unheard? *Transnational Legal Theory* 7(3), 383–405; Williams, Z.P. (2016). Investor-state arbitration in domestic mining conflicts. *Global Environmental Politics* 16(4), 32–49.



understand—and address—investment relations. It can also offer insights on rethinking the investment treaty regime and its articulation with other international norms, including environmental and human rights.

Law and the political economy of extractivism

In resource-dependent countries, extractive activities have a deep relation with statehood: public authorities often depend heavily on resource revenues and, at a deeper level, the allocation of resource rights provides an avenue for the state to exercise “effective occupation” and thus assert sovereignty under international law.⁴ Commodities such as petroleum, gold, and palm oil can sustain mythologies of national identity and development, as well as exports and foreign exchange. Natural resource governance may involve extensive public contestation over development pathways and diverse combinations of cooperation and resistance on the part of groups affected by extractive activities.

Though governance patterns vary greatly, certain features tend to facilitate large-scale projects. State institutions often control natural resources and have the power to allocate them to prospective investors. Diverse legal arrangements encourage commercial investments while marginalizing local resource rights that may impede them. For example, broad or ill-defined notions of “public purpose” can enable authorities to expropriate land and award rights to extractive projects, in effect prioritizing certain private activities over others.⁵ Also, some laws make land rights conditional on proof of “productive use,” with skewed notions of productivity—often measured solely in terms of durable land use change—weakening the rights of shifting cultivators, pastoralists, and hunter gatherers.⁶

Often rooted in colonial legacies, such arrangements facilitate investment in activities that, through elaborate webs of contracts, integrate extraction sites into the

global economy. They are embedded in variable political economies that link the state to national elites pursuing public or personal interests in resource extraction; export markets needing secure commodity supplies; foreign capital in search of business opportunities; international financial institutions supporting or imposing business-friendly policy reform; and local actors, such as traditional authorities, mediating access to resource-rich locations.⁷ These arrangements are among the root causes of conflicts associated with expanding the extractive frontier to areas without a history of large-scale investments because the law undermines the traditional bond people feel toward the territory they inhabit. Instead, it prioritizes the allocation of resource rights to commercial operators. In such legal contexts, even investments that comply with national law can systematically impair local resource claims.

"Often rooted in colonial legacies, such arrangements facilitate investment in activities that, through elaborate webs of contracts, integrate extraction sites into the global economy. "

Disputes often arise from a skewed distribution of costs and benefits, as well as the material dispossession and social dislocation that new large-scale projects can impose on local actors. But they can also originate from the deeper transitions such projects represent, with commercial and national development imperatives taking precedence over the social, cultural, and spiritual values many people attach to their surrounding environment. With so much at stake, investment disputes can provoke tense conflicts between businesses, people whose ways of life are at stake, and diverse national and local government agencies, as well as divisions within and between communities.

⁴ Weinar, L. (2016). *Blood oil: Tyrants, violence, and the rules that run the world*. Oxford University Press, at 67–79.

⁵ See, e.g., Gebremichael, B. (2016). Public purpose as a justification for expropriation of rural land rights in Ethiopia. *Journal of African Law* 60(2), 190–212. On the interface between land and subsoil resource rights, see Bastida, A.E., (2020). *The law and governance of mining and minerals: A global perspective*. Hart, pp. 161–163.

⁶ See, e.g., Nguiffo, S., Kenfack, P.E., & Mballa, N. (2009). *The influence of historical and contemporary land laws on indigenous peoples' land rights in Cameroon*. Forest Peoples Programme. <http://www.forestpeoples.org/en/topics/rights-land-naturalresources/publication/2010/land-rights-and-forest-peoples-africa-2-camero>.

⁷ See also Bebbington, A., Abdulai, A.-G., Humphreys Bebbington, D., Hinfelaar, M., & Sanborn, C.A. (with J. Achberger, C. Grisi Huber, V. Hurtado, T. Ramirez & S.D. Odell). (2018). *Governing extractive industries: politics, histories, ideas*. Oxford University Press. <https://fdslive.oup.com/www.oup.com/academic/pdf/openaccess/9780198820932.pdf>.



The place of international law

International law provides the legal foundation for extractive strategies. It organizes people and territories into states,⁸ and vests with states “permanent sovereignty” over natural resources located within their jurisdiction.⁹ International law requires that states exercise their sovereignty “in the interest ... of the well-being of the people.”¹⁰ A country’s population typically hosts divergent interests and aspirations, and states have the legal authority to reconcile these interests and represent them on the international plane. In practice, empirical accounts highlight the diverse interests that different state institutions may advance,¹¹ while international norms on issues such as human rights, Indigenous Peoples, and environmental governance affirm the pluralistic nature of real-life political organization.

International law creates obligations for states and offers redress for violations, enabling non-state actors to mobilize the language of international law when attempting to influence public authorities. Recourse to international law in natural resource disputes has also resulted in actual legal proceedings aimed at holding states accountable for alleged violations, including human rights litigation and investor–state arbitrations. Such proceedings often arise from difficult disputes where different universes collide—from corporate boardrooms to the traditional ways of life of people who hold a strong connection to their land and territory.

Due to the social and legal contexts from which they originate, proceedings can expose tensions between local and international constructs, and between different international norms. For example, international human rights litigation may require petitioners to reframe their resource claims into notions, such as the human right to property, that conflict with Indigenous conceptions. And while human rights jurisprudence has tied people’s relationship with territory to traditional cosmovisions, self-determination

and the realization of socioeconomic rights,¹² investment protection norms mainly conceptualize natural resources as commercial assets, with their value expressed in monetary terms.

Tensions within international law are particularly apparent in cases where human rights and investment treaties protect competing resource claims. In litigation before the Inter-American Court of Human Rights, Indigenous Peoples have challenged the handling of land restitution and the awarding of commercial concessions. Such claims can come into conflict with investment protection norms. In *Sawhoyamaxa Indigenous Community v. Paraguay*, for example, an Indigenous community sought restitution of land owned by a foreign investor protected under a bilateral investment treaty.¹³ Conversely, in several investor–state arbitrations, businesses have challenged actions states claimed to have taken, at least in part or in the rhetoric, to address local concerns or unrest about a project’s impact, while states or non-disputing parties have developed human rights arguments to persuade the arbitral tribunal to reject investor claims. In *Bear Creek v. Peru*—to cite but one example—the tribunal discussed the implications of consultation requirements established by international legal instruments protecting Indigenous Peoples’ rights, ultimately reaching split conclusions on both law and facts.¹⁴

Systemic integration—and problems

On one level, international law provides tools to manage these tensions. For example, “systemic integration” requires tribunals to consider other relevant, applicable rules of international law when interpreting a treaty.¹⁵ Arbitral tribunals have recognized that investment treaties are part of wider international law, and in some cases they have applied systemic integration to consider human

⁸ Eslava, L. & Pahuja, S. (2020). The state and international law: A reading from the Global South. *Humanity* 11(1), 118–138, 145–146.

⁹ United Nations General Assembly Resolution 1803 (XVII) of 14 December 1962.

¹⁰ *Ibid.*, para. 1.

¹¹ Sands, A. (2020, Dec. 21). *Unpacking regulatory chill: the case of mining in the Santurbán Paramo in Colombia*. International Institute for Environment and Development, <https://www.iied.org/unpacking-regulatory-chill-case-mining-santurban-paramo-colombia>.

¹² See, e.g., the following judgments of the Inter-American Court of Human Rights: *Yakye Axa Indigenous Community v. Paraguay* (2005), at 124, 131, 135; *Saramaka People v. Suriname* (2007), at 82, 93, 95; and *Kichwa Indigenous People of Sarayaku v. Ecuador* (2012), at 145–146, 155, 176.

¹³ *Sawhoyamaxa Indigenous Community v. Paraguay*, Inter-American Court of Human Rights, Judgment (2006), paras. 115(b), 125, 137. See more generally Van Ho, T. (2016). Is it already too late for Colombia’s land restitution process? The impact of international investment law on transitional justice initiatives. *International Human Rights Law Review* 5(1), 60–85.

¹⁴ *Bear Creek Mining Corporation v. Republic of Peru*, Award (30 November 2017), paras. 203, 208, 257–264, 406–412, 565–569, 656–668, and Partial Dissenting Opinion of Professor Philippe Sands QC (12 September 2017).

¹⁵ Article 31(3)(c) of the Vienna Convention on the Law of Treaties (Vienna, 23 May 1969), 1155 U.N.T.S. 331.



rights.¹⁶ Systemic integration does not, however, change the scope of a tribunal's jurisdiction, and leaves considerable room for discretion—for instance on which rules are relevant and how to take them into account. It also raises the question of whether investment tribunals are well placed to interpret human rights law.

More fundamentally, tensions between human rights and investment law arguments reflect systemic problems rather than isolated incidents; addressing them requires more than techniques coordinating the interpretation of international norms. Recourse to human rights is often a response to the structural marginalization that local actors face in national governance, which can result in authorities allocating concessions with little consultation or compensation, let alone respect for local resource rights and systems of belief. Meanwhile, public mobilization against an investment project perceived to have been approved without due consultation can lead to protests, government action aimed at cancelling or renegotiating the project, and, ultimately, investor–state arbitration.

"More fundamentally, tensions between human rights and investment law arguments reflect systemic problems rather than isolated incidents; addressing them requires more than techniques coordinating the interpretation of international norms."

These considerations point to a misalignment between the nature of disputes and the international rules and procedures in place to settle them. While natural resource disputes often involve multiple actors and raise wide-ranging issues, the jurisdiction of investor–state arbitral tribunals primarily centres on whether a state breached certain standards of treatment owed to foreign investors. This narrows the bounds of the dispute and sidelines other arguments such

as those based on human rights—relegating them, for example, to discussions about the amount of damages a state must pay a business.¹⁷ Local activists can, and often do, take their own claims to national courts, international human rights institutions, and grievance mechanisms established by lenders or commodity bodies, and lack of coordination between arrangements addressing investment claims and human rights claims can fragment dispute settlement proceedings and outcomes.

Investment law's distributive implications

In complex natural resource disputes, the narrow framing of investment law has distributive consequences, structurally marginalizing local actors whose rights may be directly at stake—from people suffering land dispossession or environmental damage to prospective agrarian reform beneficiaries. Procedurally, actors who may have challenged the state's policies in the streets or even in court must now rely on state agencies to represent their perspectives. Though applicable arbitration rules may allow them to make *amicus curiae* submissions, these are merely one-off, informational contributions to assist the tribunal in its deliberations. Tribunals enjoy wide discretion on whether to accept these submissions and what use, if any, to make of the arguments they contain. Restricted access to case documents or hearings makes it difficult for the *amici* to calibrate their arguments, reducing the likelihood the tribunal will consider them.¹⁸ As a result, local perspectives are typically “invisible” in dispute settlement proceedings.¹⁹

The investment treaty regime also matters in substantive terms, as it can affect both the range of protected interests and the strength of legal protection. By elevating to the international plane the rights and interests of certain private actors, without qualifying them with

¹⁶ E.g., *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic*, ICSID Case No. ARB/07/26, Award (8 December 2016), paras. 1190, 1200, 1204.

¹⁷ *Copper Mesa Mining Corporation v. The Republic of Ecuador*, PCA Case No. 2012-2, Award (15 March 2016).

¹⁸ In *Pac Rim Cayman LCC v. Republic of El Salvador*, ICSID Case No. ARB/09/12, Award (14 October 2016), the tribunal deemed it “unnecessary” to engage with the arguments contained in an *amicus curiae* submission, noting that the petitioners were “not privy to the mass of factual evidence adduced in this arbitration’s third phase, including the hearing” (para. 3.30).

¹⁹ Perrone, N.M. (2018). The “invisible” local communities: Foreign investor obligations, inclusiveness, and the international investment regime, *AJIL Unbound* 113:16–21.



commensurate obligations,²⁰ it alters the balance of rights and obligations between transnational businesses, state agencies, and local actors. For example, although the acquisition of natural resource rights is typically regulated by national law, international law protects investor interests that national law does not necessarily recognize as legal rights. Indeed, arbitral tribunals have interpreted investment treaties as protecting investors' "legitimate expectations," which public officials can create if, for example, they give assurances that land is available and the necessary permits will be issued.

Should officials make such representations before consulting affected people, tensions may arise between investor expectations and local resource rights. By converting investor expectations into legal claims, the legitimate expectations doctrine can shift the balance between these competing interests.²¹ Compensation is the most common remedy in investor–state arbitration, meaning states can safeguard local rights and compensate investors. But arbitration proceedings can directly affect third-party rights, for example where an investor seeks relief that interferes with the enforcement of judgments third parties secured in national courts,²² and the risk of an expensive dispute may discourage the state from acting in the first place.²³

While local actors may be able to resort to international human rights institutions, investment treaties provide foreign investors with further-reaching and more readily enforceable protections. Unlike investment treaties, human rights instruments require actors to exhaust domestic remedies before accessing international redress, which can take years of litigation before national courts. Asymmetries can also result from substantive or review standards. For example, the European Court of Human Rights held that states enjoy a "margin of appreciation" in applying international norms, defining its own remit as assessing whether

authorities have struck an overall "fair balance" between private property and public interests. By contrast, most arbitral tribunals have not followed the margin of appreciation doctrine and, in expropriation claims, have looked at whether state conduct met each of the conditions investment treaties typically require for expropriations to be lawful. Where damages are a relevant aspect, investor–state tribunals have awarded significantly higher amounts than human rights courts.²⁴ Differences are even more pronounced where no effective regional human rights court is in place.

Stronger rights and more effective means of redress may give transnational businesses greater leverage in their relations with government than that enjoyed by the people their activities affect, compounding imbalances in different actors' ability to influence public decisions. Though international law is primarily thought of as regulating international relations, it can in this way reverberate across national political arenas.

The need for a holistic approach

Debates about investment governance are a function of perspective and positionality. Legal experts advising transnational businesses may be concerned about state action undermining commercial returns. They may perceive the questioning of the investment treaty regime as a process of economic disintegration, with states rolling back legal arrangements governing cross-border investment.²⁵ But for many people affected by resource extraction, it is the prevailing legal regime that dis-embeds and disintegrates, because investment treaties can protect ventures that, while consistent with national law, upend their lives with little scope for voice or redress.

Tackling these issues requires holistic consideration of multiple spheres of national and international law—examining the investment treaty regime not in isolation but as it intersects with, and affects, wider governance arrangements. In policy terms, it calls for systemic change well beyond investment treaties.

²⁰ For a discussion, see Gathii, J. & Puig, S. (2019). Introduction to the symposium on investor responsibility: the next frontier in international investment law, *AJIL Unbound* 113:1–3.

²¹ Johnson, L. (2017–2018). A fundamental shift in power: Permitting international investors to convert their economic expectations into rights. *UCLA Law Review Discourse* 65, 106–123.

²² Sachs, L., Johnson, L., Merrill, E. (2020). Environmental injustice: How treaties undermine human rights related to the environment. *Revue des Juristes de Sciences Po* 18, 90–100.

²³ For a discussion, see Tienhaara, K. (2018). Regulatory chill in a warming world: The threat to climate change policy posed by investor-state dispute settlement. *Transnational Environmental Law* 7(2), 229–250.

²⁴ See, e.g., De Brabandere, E. (2015). Complementarity or conflict? Contrasting the Yukos case before the European Court of Human Rights and investment tribunals. *ICSID Review* 30(2), 345–355.

²⁵ Montanaro, F. & Violi, F. (2020). The remains of the day: The international economic order in the era of disintegration. *Journal of International Economic Law* 23(2), 299–322.



Depending on the context, national law reforms may be necessary to protect traditional resource rights and facilitate public participation in investment approval, while the ongoing negotiation of a multilateral treaty on business and human rights could help rebalance rights and obligations.

As for international investment law, options range from terminating old treaties to reforms that redesign investment protections, affirm investor obligations, for example on the environment and human rights, and exclude from protection investments that fail to comply.²⁶ Reformist options also include reimagining dispute settlement to more effectively consider the rights of people affected by an investment or dispute, not just in procedural terms, but also through dismissal or reframing of investor claims as circumstances require.²⁷ Institutional cross-linkages could improve coherence within international law—for example, through conflict provisions establishing the primacy of human rights obligations over investment treaties, and mandating that arbitral tribunals refer to human rights bodies any issues that require interpretation of human rights law.²⁸

At a time when legal professionals are under pressure to specialize in ever-narrower fields, effective responses require a “big-picture” view of the multiple bodies of law involved and imaginative action at local to global levels.

Author

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²⁶ See also Surya Deva, “Managing States’ ‘Fatal Attraction’ to International Investment Agreements” (13 August 2018) *Investment Policy Hub*, <https://investmentpolicy.unctad.org/blogs/75/managing-states-fatal-attraction-to-international-investment-agreements->.

²⁷ These points are articulated in CCSI, IIED and IISD, *Third Party Rights in Investor-State Dispute Settlement: Options for Reform* (submission to UNCITRAL Working Group III on Investor-State Dispute Settlement Reform, 2019), <http://ccsi.columbia.edu/files/2019/07/uncitral-submission-third-party-participation-en.pdf>.

²⁸ Markus Krajewski, *Ensuring the Primacy of Human Rights in Trade and Investment Policies: Model Clauses for a UN Treaty on Transnational Corporations, Other Businesses and Human Rights* (CIDSE, 2017), https://www.cidse.org/wp-content/uploads/2017/03/CIDSE_Study_Primacy_HR_Trade_Investment_Policies_March_2017.pdf; Jesse Coleman, Kaitlin Y. Cordes and Lise Johnson, “Human Rights Law and the Investment Treaty Regime” CCSI Working Paper (2 June 2019) <http://ccsi.columbia.edu/files/2019/06/Coleman-Cordes-and-Johnson-Human-Rights-Law-and-the-Investment-Treaty-Regime.pdf>. On institutional coordination between human rights bodies and the investment treaty regime, see also Bruno Simma and Diane Desierto, “Bridging the Public Interest Divide: Committee Assistance for Investor-host State Compliance with the ICESCR” (2013) *Transnational Dispute Management* 1.



INSIGHT 2

Corruption and confidentiality in contract-based ISDS: The case of *P&ID v Nigeria*¹

Jonathan Bonnitcha



In September 2020, the English High Court handed down a key decision in the case *P&ID v Nigeria*. The court was considering Nigeria’s attempt to overturn a USD 10 billion award rendered in an arbitration under a contract between a foreign investor and Nigeria.² Although Nigeria did not raise allegations of corruption during the arbitration, it now alleges that the investor obtained the underlying contract by bribing Nigerian officials and that the investor subsequently bribed Nigeria’s legal counsel to ensure that the country would not contest the arbitration vigorously. The court found there was a “strong prima facie case” that the contract was procured by bribes and that the investor’s main witness in the arbitration gave perjured evidence.³ It further found there was

a possibility that Nigeria’s legal counsel in the case had been corrupted.⁴ The effect of this judgement is that these issues can now proceed to a full hearing, to determine whether the award should be set aside, which is unlikely to take place until 2022.

Regardless of whether the allegations of corruption in this particular case are true, the saga highlights wider policy concerns about the way that investor–state arbitration intersects with corruption. Given the significant public interests at stake in investor–state arbitration, including the possibility that arbitration may facilitate the corrupt transfer of public funds to private actors, they should not be conducted in private. In addition to the concerns about the lack of transparency in contract-based investor–state arbitration, the case raises more profound questions about whether arbitration is ever an appropriate forum for resolving investor–state disputes.

Background to the arbitration

In 2010, the Nigerian Ministry of Petroleum Resources signed a contract for the construction and operation of a new gas processing facility with P&ID, a company incorporated in the British Virgin Islands.

Under the contract Nigeria was to supply natural gas (“wet gas”) at no cost to P&ID’s facility. For its part, P&ID was to construct and operate the facility. It would process the gas to remove natural gas liquids—which P&ID was entitled to—and return lean gas to Nigeria at no cost, which would be suitable for use in power generation and other purposes.⁵

¹ This article draws on a longer research collaboration. See Bonnitcha, J. & Mathew, A. (2020). *Corruption in investor-state arbitration*. Transparency International. <https://knowledgehub.transparency.org/helpdesk/corruption-in-investor-state-arbitration>. However, the views expressed here are those of the Transparency International Knowledge Hub present author and not those of Transparency International or any other person or organization.

² The dispute has been the subject of detailed investigative reporting by Bloomberg and the Financial Times. See “The \$6bn judgment pitting Nigeria against a London court.” (2020.) <https://www.bloomberg.com/news/features/2019-09-04/is-one-of-the-world-s-biggest-lawsuits-built-on-a-sham> <https://www.ft.com/content/91ddb53-a754-4190-944e-d472921bb81e>

³ *Federal Republic of Nigeria v Process & Industrial Developments Limited* [2020] EWHC 2379 (Comm), para 226.

⁴ *Ibid.*, para 225.

⁵ *Ibid.*, para 21.



Both the contract and the circumstances relating to its conclusion were unusual. For one, the contract was based on an unsolicited proposal presented to the Nigerian government by P&ID.⁶ No tender was conducted. Moreover, P&ID did not appear to have the experience in the gas sector that would be expected of a company responsible for a multibillion-dollar project—it was an offshore entity with “no assets, only a handful of employees, and was without a website or other presence.”⁷

Under clause 20 of the contract, the parties agreed that the contract was governed by Nigerian law and that disputes under it would be resolved through arbitration at the “venue” of London, England.⁸ In August 2012, P&ID initiated arbitration, alleging that Nigeria had repudiated the contract. At that time, P&ID had not commenced construction of the facility or even purchased a site on which the facility could be built.⁹ Nevertheless, P&ID argued that it stood ready to carry out its obligations under the contract and that the project foundered due to Nigeria’s failure to perform its side of the deal.

As is common in contract-based investor–state arbitration, the arbitration was conducted in private. Indeed, even the fact that the arbitration was taking place did not become public knowledge until 2015, following a change of government in Nigeria, at which point in time the jurisdictional and merits phases of the arbitration had already concluded. Despite a number of “red flags” of corruption relating to the contract,¹⁰ Nigeria did not directly raise the issue of corruption in its defence of the arbitration. (Nigeria’s lawyers in the arbitration did obliquely describe the Minister of Petroleum Resources at the time the contract was signed “as having been a ‘friendly’ Minister who purported to commit the Government to obligations and concessions which exceeded his

powers.”¹¹) Based on documents that are publicly available, it seems that the tribunal also did not take any steps to determine whether the contract might have been procured through corruption.

Given the many billions of dollars at stake, the way the arbitration unfolded was also unusual. Nigeria’s lawyers failed to file expert evidence on jurisdictional issues of Nigerian law,¹² or insist on an oral hearing on jurisdiction where P&ID’s evidence might have been tested through cross-examination.¹³ At the merits phase, Nigeria failed to challenge the key claims contained in the statement of P&ID’s central witness, its chairman, Michael Quinn.¹⁴ It put forward only one ineffectual witness of its own who did ‘not claim to have first-hand knowledge of any of the relevant events.’¹⁵ The tribunal did hold a hearing on the merits, but it lasted only a few hours.¹⁶ The tribunal concluded that Nigeria had repudiated the contract.

The tribunal’s decision on quantum was based on a single witness statement from the investor. It did not order the production of documents that might have proved (or disproved) these self-serving claims.¹⁷ On the strength of the investor’s evidence, it awarded P&ID USD 6.6 billion in damages plus interest of 7% p.a. The size of the award is extraordinary, given that the investor had not commenced construction of the gas facility and estimated its own expenditure in relation to the project at around USD 40 million.¹⁸ (In the subsequent British court proceedings, the investor conceded that this expenditure had not been incurred by P&ID at all but, rather, by another company owned by a former Nigerian general.)¹⁹

⁶ *P&ID v Nigeria*, Part Final Award on Liability, ¶37(e) (Jul. 15, 2015).

⁷ *Supra* note 3, para 6.

⁸ *P&ID v Nigeria*, Part Final Award on Jurisdiction, ¶ 7 (Jun. 3, 2014).

⁹ *Supra* note 3, para 209.

¹⁰ The term “red flags” refers to circumstantial evidence that suggests possible corruption. The existence of red flags does not necessarily mean a transaction was corrupt but, rather, points to the need for further inquiries to determine whether a transaction was corrupt: Sayne, A., Gillies, A., & Watkins, A., (2017). *Twelve red flags: Corruption risks in the award of extractive sector licenses and contracts*. Natural Resource Governance Institute <https://resourcegovernance.org/sites/default/files/documents/corruption-risks-in-the-award-of-extractive-sector-licenses-and-contracts.pdf>

¹¹ *Supra* note 6, ¶41 (Jul. 15, 2015).

¹² *Supra* note 8, ¶ 33. (Jun. 3, 2014).

¹³ *Ibid.*, ¶¶ 30–31 (Jun. 3, 2014).

¹⁴ *Ibid.*, ¶ 29 (Jun. 3, 2014).

¹⁵ *Supra* note 6, ¶ 68 (Jul. 15, 2015).

¹⁶ *Supra* note 3, para 52.

¹⁷ *Supra* note 3, para 205.

¹⁸ First Witness Statement of Michael Quinn, 10 February 2014, para 47.

¹⁹ *Supra* note 3, para 204.



Nigeria's attempt to set aside the award in English courts

The arbitral tribunal's award triggered further litigation in several jurisdictions. However, it was not until November 2019 that Nigeria first raised allegations of corruption in an attempt to convince English courts to set aside the award. As the arbitral tribunal had interpreted the contract as designating London as the seat of the arbitration, English courts had jurisdiction to hear challenges to the award by way of an application to set it aside. Corruption is one of a handful of grounds on which an English court has the power to set aside an arbitral award.²⁰ If Nigeria does ultimately succeed in getting the award set aside, it will become nearly impossible for P&ID to enforce the award anywhere in the world.

The immediate challenge for Nigeria was that the deadline for commencing proceedings to set aside an award in English courts is 28 days from when the award was rendered. Nigeria had missed this deadline by almost three years. In this context, the English court had to consider whether there was enough prima facie evidence of corruption to justify granting Nigeria an exceptional and unprecedented extension of time in bringing its application to set aside the award.

In clearing this high bar, Nigeria was assisted by new evidence obtained through an application for discovery of banking records made in New York earlier in 2020.²¹ As a result of disclosure orders made by the U.S. court, Nigeria was able to introduce evidence of bank transfers to Nigerian government officials that had been made by entities affiliated with P&ID,²² as well as evidence of large, unexplained cash withdrawals from a P&ID affiliated entity's Nigerian bank account around the time the contract was signed.²³ This evidence, when considered in light of the many other unusual aspects of the case, led to the court's conclusion that there was a 'strong prima facie case' that the contract was procured by bribes and the granting of an extension of time.

Is private arbitration an appropriate forum for resolving investor–state disputes?

The fact that questions of corruption are being litigated now, almost a decade after the arbitration began, is hardly an ideal outcome. That a USD 10 billion award obtained in these circumstances came so close to being enforced without the question of corruption being examined is even more alarming. The burden of paying such an award would fall on Nigeria's citizens and taxpayers, not on the government officials involved in the allegedly corrupt transaction.

Regardless of whether Nigeria's allegations of corruption are ultimately substantiated, the case of *P&ID v Nigeria* points to two related concerns about arbitration as a method for resolving disputes between states and investors. The first concern relates to confidentiality in contract-based investor–state arbitration. As was the case in *P&ID v Nigeria*, such arbitrations are normally conducted in private. This prevents timely public scrutiny. Such scrutiny might increase the pressure on a state to provide an account of its own conduct, including the circumstances in which a contract with a foreign investor was negotiated and concluded. In the case of *P&ID v Nigeria*, for example, it's hard to imagine that questions about corruption could have been avoided for so long if the public had known that a foreign investor was seeking billions of US dollars compensation for a gas processing facility that was never built. Greater transparency might also lead to the intervention of third parties, with new evidence, in the dispute.

"it's hard to imagine that questions about corruption could have been avoided for so long if the public had known that a foreign investor was seeking billions of US dollars compensation for a gas processing facility that was never built."

²⁰ Arbitration Act (1996) section 68(2)(g)

²¹ *Supra* note 3, paras 111–112

²² *Supra* note 3, paras 196–199.

²³ *Supra* note 3, para 191



The 2014 UNCITRAL Rules on Transparency in Treaty-Based Investor–State Arbitration provide a model for what greater transparency in contract-based investor–state arbitration could look like.²⁴ These rules establish default presumptions in favour of transparency, subject to limited exceptions – for example, to protect against disclosure of confidential business information. The fact that equivalent transparency rules do not yet apply in contract-based investor–state arbitrations reflects idiosyncrasies in the way the transparency debate evolved over time; it is not a result of considered arguments that *contract-based* investor–state arbitration should be exempt from the same level of transparency that applies in *treaty-based* investor–state arbitration.

Second, the case of *P&ID v Nigeria* points to wider concerns about arbitration as a forum for the resolution of investor–state disputes. In particular, there is a tension between the political economy of corruption and doctrines, disciplinary practices, and embedded assumptions in the field of arbitration. These include that:

- Arbitration is a mechanism for resolving disputes based on parties’ consent. For this reason, tribunals have historically confined themselves to deciding issues raised by the parties. This means that tribunals tend not to consider the possibility of corruption, unless a clear allegation is made by one of the parties to the disputes.
- Lawyers and officials representing the state in an arbitration may themselves be the beneficiaries of corruption or be subject to institutional constraints that prevent them from speaking out. For this reason, the fact that those representing the state have not raised allegations of corruption does not mean a transaction was legitimate.
- International legal doctrine tends to see the state as a unitary actor, rather than a site of political contestation between groups. These habits of thought can encourage arbitrators to attribute corruption and incompetence on the part of government officials to the state itself. This way of seeing the world makes arbitrators less sympathetic to a state’s allegations of bribery on the part of the investors when such allegations are raised, because such allegations can be perceived as a state raising *its own* misconduct in having accepted a bribe to defeat a claim against it.
- International arbitrators have a tendency to view arguments based on the law of the host state as technical and irrelevant, even if the purpose of such laws is to prevent corruption or implement a system of oversight over decisions relating to public resources.

There are no easy solutions to these challenges within the existing framework of investor–state arbitration. On this basis, states may wish to go further and consider whether contract disputes are more appropriately resolved in courts than through arbitration.

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²⁴ UNCITRAL. (2014). UNCITRAL rules on transparency in treaty-based investor-state arbitration. <https://www.uncitral.org/pdf/english/texts/arbitration/rules-on-transparency/Rules-on-Transparency-E.pdf>.



INSIGHT 3

On proportionality, again: Domesticating international investment law and managing vulnerability¹

Daria Davitti



Proportionality has been proposed as a panacea to resolve many of the tensions between international investment law (IIL) and international human rights law (IHRL) when foreign investment adversely impacts the human rights of host states' communities, and host states encounter competing international law obligations. However, there seems to be a need to revive these debates, since the allure of proportionality is alive and well in both the negotiations for a [binding instrument on business and human rights](#) and in the work of [UNCITRAL Working Group III on ISDS reform](#).¹ In this piece, we will first try to understand how we arrived at this discussion, yet again, within the broader debate on human rights and IIL.

The fatal attraction of balancing

The revival of proportionality relies on the appeal of achieving a “balance” between the so-called rights of investors, protected as they are by relevant IIAs, and the human rights of communities and individuals affected by foreign investment. Such balancing often

entails, at its core, a controversial juxtaposition between investment protections and human rights protections. With calls for balancing back in fashion, I return to this argument here because now, faced with climate breakdown and an escalating pandemic, we need more than ever to debunk existing assumptions surrounding the use of balancing and proportionality in international investment arbitration as a way of successfully reconciling competing interests and conflicting protection obligations vested upon host states.

The suggestion that investment tribunals will be able to effectively “balance” conflicting interests seems to flow from the argument that competing IIL and IHRL obligations can be successfully harmonized by tribunals through treaty interpretation. Scholars have indeed submitted that vague treaty-based investment protection standards can be more efficiently interpreted² by employing the principle of systemic integration to “help clarify IIA standards for the benefit of the investors” or to “elucidate the limits of investor protection and, hence, *minimize frictions* with competing public interests.”³

The mantra of balancing (or rebalancing) IHRL and IIL usually goes through two stages: first, the operationalization of IHRL through treaty interpretation; second, a different approach to foreign investment agreements according to which the human rights obligations of the host state are clarified from the outset. It is around the viability and indeed desirability of using proportionality analysis while pursuing these two pseudo-solutions that this contribution is structured, since various scholars have enthusiastically endorsed this approach over the years. Crucially, these two alternatives are also the gateway to the adoption of proportionality analysis in international investment arbitration. To

¹ This is a shorter version of a full-length article published in the *Nordic Journal of International Law* (2020) 89(3–4). The author would like to thank Paolo Vargiu, Anil Yilmaz Vastardis and Mavluda Sattarova for their insightful comments on drafts of this contribution.

² Davitti D. (2020). *Investment and human rights in armed conflict. Charting an elusive intersection*. Hart Publishing.

³ Shill, S. & Djanic V. (2018). Wherefore art thou? Towards a public interest-based justification of international investment law. *ICSID Review - Foreign Investment Law Journal* 33(1), 29–55.



reconcile investment protection and human rights, some propose the **drafting** of rights-friendly IIA clauses, arguably capable of addressing the asymmetric character of the system.⁴ Such clauses, it is alleged, would ensure that human rights are taken into consideration by international investment tribunals and foreign investors alike. Reliance on treaty interpretation and rights-friendly drafting, in my view, has revealed itself to be both misplaced and short-sighted.⁵ These approaches, I argue, focus on the *domestication* of IIL and on the *management of vulnerability*,⁶ rather than on ensuring that the actual rights of the communities affected by foreign investment are effectively respected, protected and fulfilled.

Is a “balancing” possible? On managing vulnerability

This question is not to be understood as a mere rhetorical point. Proponents of balancing suggest that IHRL can be brought to bear in the interpretation of the relevant international investment treaty through the “principle of evolutionary, or dynamic, interpretation” provided that the parties intended the possibility for the meaning of a certain term to change in future.⁷ On the basis of this reasoning, international law can be used to determine the meaning of a specific term when the treaties in question use “known legal terms whose content the parties expected would change through time.”⁸ International law will then be referred to on the basis of its evolution and current status, rather than considering the state of the law at the time of the conclusion of the treaty. Furthermore, an additional way in which IHRL can be considered as relevant to the investment treaty in question is through

the interpretative presumption that treaties are intended to produce effects which accord with **existing rules of international law**. This presumption is used to resolve issues of interpretation relating to the **broader normative content** of a treaty rather than to the meaning of a specific term.⁹

The key tool for IHRL to be considered in the interpretation of an international investment treaty, so the argument goes, is Article 31(3)(c) of the **VCLT**, which in turn represents a means of treaty interpretation rather than a potential instrument to modify the scope and content of a treaty, for instance, to introduce ex novo human rights consideration. It goes without saying, therefore, that supporters of evolutionary interpretation—despite acknowledging that investment treaty arbitration is unable to respond to the challenge of harmonization—are happy to leave the status quo of IIL as a system practically fundamentally unchallenged.

This means that human rights and environmental vulnerability are thus better “managed” through the ultimate discretion of investment treaty arbitrators or newfound “courts,” within a system that, in itself, is both ideologically and practically inappropriate to review a state’s exercise of its regulatory powers. If we think about it for a moment, what is it really that we would like these adjudicators to “balance”? A recent report by IIED reveals that, of a dataset of 257 coal power plants owned by foreign investors, at least 75% are protected by at least one IIA which provides investors with access to international investment arbitration.¹⁰ At a time when efforts to halt climate breakdown inevitably rely on our ability to promptly abandon fossil fuel dependency, IIAs legally encode investors’ rights to compensation whenever states might seek to decommission any of these coal power plants.¹¹ This state of affairs is sufficient to raise concerns in relation to regulatory chill and intergenerational equity, but should be further considered together with recently emerged evidence that in the 1980s major fossil fuel companies already predicted the damage that their products would cause, systematically downplayed scientific evidence on the links between fossil fuel consumption and climate change, and lobbied to delay and obstruct the introduction of climate legislation.¹² Litigation is already emerging in relation to policy measures aimed at phasing out coal power stations, not least under the ECT.¹³

⁴ Arcuri, A. & Montanaro F. (2018). Justice for all? Protecting the public interest in investment treaties. *Boston College Law Review*. 59(8). <https://lawdigitalcommons.bc.edu/bclr/vol59/iss8/10/>

⁵ Sattorova, M., Erkan, M., & Omiuno, O. (2019). How do host states respond to investment treaty law? Some empirical observations. In M. Sattorova, (Ed.), *European Yearbook of International Economic Law*. Hart Publishing.

⁶ Eslava, L. & Buchely, L. (2018). Security and development? A story about petty crime, the petty state and its petty law. *Revista de Estudios Sociales*. <https://revistas.uniandes.edu.co/doi/full/10.7440/res67.2019.04>

⁷ Simma, B. (2011). Foreign investment arbitration. A place for human rights? *International & Comparative Law Quarterly*, 60, p. 538

⁸ Simma, supra note 7, p. 583. See also *Legal consequences for states of the continued presence of South Africa in Namibia (South West Africa) notwithstanding Security Council Resolution 276 (1970)*. <https://www.icj-cij.org/en/case/53>

⁹ Simma, supra note 7, p. 583

¹⁰ Tienhaara, K. & Cotula, L. (2020). *Raising the cost of climate action? Investor-state dispute settlement and compensation for stranded fossil fuel assets*. IIED Land, Investment and Rights Series. <https://pubs.iied.org/sites/default/files/pdfs/migrate/17660IIED.pdf>

¹¹ Pistor, K. (2019). *The code of capital. How the law creates wealth and inequality*. Princeton University Press.

¹² See, e.g., Franta, B. (2018). Shell and Exxon’s secret 1980s climate change warnings. *The Guardian*. <https://www.theguardian.com/environment/climate-consensus-97-per-cent/2018/sep/19/shell-and-exxons-secret-1980s-climate-change-warnings>; Influence Map. (2016). *An investor enquiry: how much big oil spends on climate change lobbying*. https://influencemap.org/site/data/000/173/Lobby_Spend_Report_March_2016.pdf

¹³ Khan M. (2021). EU urged to quit energy treaty. *Financial Times*. <https://www.ft.com/content/b37312fb-410a-4958-a887-8f9bd7c5e33b>



Despite this damning scenario, proponents of balancing, or vulnerability managers, as I choose to call them here, would promptly point to the fact that defences and exceptions could certainly be used by international investment adjudicators to recognize the claims of host states and affected communities alike. Meanwhile, major corporate actors continue to lobby against climate change regulation and purport to support carbon emissions reduction measures in return for legal immunity from liability for historic emissions. In light of the above, and of the mounting scientific evidence that we perhaps have 10 years to limit the devastating consequences of climate warming,¹⁴ I am sure I am not alone in feeling uncomfortable in thinking that “balancing” is all we have to ensure human rights and environmental protection under current circumstances.

Rights-friendly IIA clauses: On the domestication and legitimization of IIL

The same disquiet is true in the face of renewed calls for negotiating rights-friendly investment agreements. Environmental, social, and governance (ESG) audits and standards are all the rage, as newly crafted due diligence assessment tools to ensure that investment is not only sustainable but also conscientious. Scholars have indeed raised the challenge of rights-friendly drafting in the hope that these could address the asymmetric nature of IIL and ensure that human rights are properly taken into consideration in international investment arbitration. Recent examples of arbitral tribunals’ interpretation of human rights clauses, however, demonstrate that the design of rights-friendly IIA and investment contracts is insufficient to ensure human rights protection. Some awards have been celebrated as a victory for the host state¹⁵ or as breaking new ground¹⁶ for human rights protection in IIL, but in fact they effectively expanded and amplified protections granted to investors under IIL. This is particularly true of cases in which international investment tribunals

have considered matters of public health,¹⁷ the right to water,¹⁸ access to medicines,¹⁹ and Indigenous People’s rights.²⁰ In relation to these cases, understandable issues of legitimacy have been raised when it became apparent that crucial issues concerning the public good were, in the best of cases, reduced to a matter of policy prioritization or of quantum of compensation.

Thus, no matter how skilful the drafting and how elaborated the clauses, effective human rights protection through IIA drafting will mainly remain contingent upon tribunal interpretation²¹ in a system that is not appropriately placed to carry out public review functions.²² More specifically, when it comes to human rights and environmental protection, it is clear that this cannot be realized in a forum mandated to provide remedies for breaches of standards of investment protection, where proportionality analysis becomes a creative tool of interpretation to limit the regulatory space of host states. At the same time, proportionality is also used to justify and maintain the relevance of the investment legal system itself.²³ As we have seen, proposals for innovative investment treaty or **contract design** continue to be put forward as a possible way to **guide** investment tribunals’ interpretation, by bringing human rights considerations to bear via systemic integration and IIA drafting, including through the use of proportionality analysis. As argued in this piece, however, rather than ensuring meaningful human rights protection, these proposals risk contributing to a broader project aimed at the domestication and legitimization of IIL and at the management, rather than the eradication, of vulnerability.

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¹⁴ Letzer, R. (2019). Are we really running out of time to stop climate change? *Live Science*. <https://www.livescience.com/12-years-to-stop-climate-change.html>

¹⁵ *Philip Morris Brand Sàrl (Switzerland), Philip Morris Products S.A. (Switzerland) and Abal Hermanos S.A. (Uruguay) v. Oriental Republic of Uruguay* ICSID Case No. ARB/10/7

¹⁶ *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Bizkaia Ur Partzuergoa v. The Argentine Republic*, ICSID Case No. ARB 07/26

¹⁷ *Philip Morris Asia Limited v. The Commonwealth of Australia*, UNCITRAL, PCA Case No. 2012-12

¹⁸ *Suez, Sociedad General de Aguas de Barcelona, S.A. and Vivendi Universal, S.A. v. Argentine Republic*, ICSID Case No. ARB/03/19

¹⁹ *Eli Lilly and Company v. The Government of Canada*, UNCITRAL, ICSID Case No. UNCT/14/2

²⁰ *Bear Creek Mining Corporation v. Republic of Peru*, ICSID Case No. ARB/14/21

²¹ E.g., *Morocco-Nigeria BIT* (2016) <https://investmentpolicy.unctad.org/international-investment-agreements/treaties/tips/3711/morocco-nigeria-bit-2016>

²² Schneiderman, D. (2018). Global constitutionalism and its legitimacy problems: Human rights, proportionality and international investment law. *Law & Ethics of Human Rights* 12(2). <https://www.degruyter.com/document/doi/10.1515/lehr-2018-0014/html>

²³ Sornarajah, M. (2015). *Resistance and change in the international law of foreign investment*. Cambridge University Press.



INSIGHT 4

The uncertain future of the Energy Charter Treaty: Belgium asks the European Court of Justice to rule on the compatibility of the modernized ECT with EU law

Stefanie Schacherer



The relationship between the ECT and EU law is characterized by complexity and legal uncertainty, especially as far Article 26, the ECT's dispute settlement mechanism and its application in an intra-EU setting is concerned. The question of whether the *Achmea* judgment's finding on the incompatibility of intra-EU investment arbitration under BITs also affects the dispute settlement mechanism under the ECT has remained unresolved.¹ Given the ongoing ECT modernization negotiations (*Editor's note: see our news brief in this edition for the latest on the progress of these negotiations*), the compatibility question receives once again special attention.

By submitting a request for an opinion to the Court of Justice of the European Union (CJEU) on the compatibility of the intra-EU application of the arbitration provisions of the ECT with the EU Treaties, Belgium seeks to solicit much-wanted clarifications.² Belgium's question specifically relates to the draft text elaborated by the EU, but whatever the Court decides concerning the draft ISDS provisions in its latest form

will also have consequences for the currently applicable version of the ECT.

The past and present of the ECT

In the 1990s, the European Commission was the key initiator of the ECT, the goal of which was to protect Western European investors after the collapse of the Soviet Union. At that time, nobody would have thought that the majority of investment claims based on the ECT will be made against EU member states. Yet to date, most disputes under the ECT have been intra-EU (i.e., claims against an EU member state brought by an investor from another EU member state).

The ECT creates a web of legal relationships between all of the 52 contracting parties, including the EU and all its member states.³ It is an intra-EU IIA among 26 EU member states (without Italy) as well as an IIA amongst the EU member states and the 26 other ECT contracting parties.⁴ Since the EU itself is a party to the agreement, it also operates as an IIA between the EU and the 26 other ECT contracting parties. Consequently, issues of incompatibility of IIAs with EU law occur in the ECT context.

The ongoing legal struggle of the EU

In the 2018 *Achmea* judgment, the CJEU held that the principle of autonomy prevents two member states from setting up an investor–state dispute settlement mechanism through a BIT *inter se*.⁵ However, as stated above, *Achmea* did not settle the controversy around the intra-EU applicability of Article 26 ECT. Following the judgment, the member states adopted two instruments:

¹ ECJ, Case C-284/16 *Slovakische Republik v Achmea BV*, EU:C:2018:158.

² See press release of 3 December 2020. https://diplomatie.belgium.be/en/newsroom/news/2020/belgium_requests_opinion_intra_european_application_arbitration_provisions

³ Australia, Belarus, Norway, and Russia signed the ECT but never ratified it. <https://www.energycharter.org/process/energy-charter-treaty-1994/energy-charter-treaty/>

⁴ Italy withdrew from the ECT in 2016, but the treaty will continue to apply for Italy due to the 20-year sunset clause, see ECT, Art 47(3).

⁵ *Achmea*, supra note 1, para. 59.



- Declaration of 15 January 2019: 22 EU member states made a common declaration in which they express the view that the intra-EU applicability of Article 26 ECT was incompatible with EU law.⁶
- Termination Agreement of 5 May 2020: 23 EU member states convey to terminate all their existing intra-BITs. However, the applicability of the ECT in the intra-EU context has not been addressed and postponed to “a later stage.”⁷ Austria, Finland, Sweden, and Ireland did not sign the termination agreement.⁸

Meanwhile, the legal struggle continues before investment tribunals, domestic courts, and the CJEU. In numerous cases under the ECT, the European Commission has tirelessly argued the incompatibility of the ECT with EU law through amicus curiae submissions.⁹ To date, these arguments have not led an investment tribunal to decline its jurisdiction. Spain has sought to set aside awards against itself in Swedish courts, such as in the cases in *Novenergia II* or *Foresight*, *Greentech* and *GWM*,¹⁰ also without success. Recently, Advocate General Saugmandsgaard Øe asserted in a preliminary reference procedure before the CJEU that Article 26 ECT does not apply to intra-EU disputes.¹¹

⁶ Declaration on the Legal Consequences of the Judgment of the Court of Justice in *Achmea* and on Investment Protection in the EU. (2019). file:///Users/s3/Downloads/190117-bilateral-investment-treaties_en-1.pdf; Finland, Luxembourg, Malta, Slovenia, and Sweden issued a collective declaration, and Hungary issued an individual declaration. All find that, at the time of the declaration, it was too early to express an opinion on the compatibility of ECT, Article 26 with the EU Treaties.

⁷ Agreement for the Termination of Bilateral Investment Treaties between the Member States of the European Union, see preamble, recital 10. <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A2020A0529%2801%29>

⁸ Even though Austria and Sweden did not sign the Termination Agreement, they have committed to terminate their BITs bilaterally. Conversely, the inaction of Finland led the Commission to initiate formal infringement proceedings against Finland. Ireland has no applicable BITs.

⁹ See, *List of observations provided by the Commission to others, e.g. arbitration courts.* <https://ec.europa.eu/competition/court/observations.html>

¹⁰ *Novenergia II - Energy & Environment (SCA), SICAR v. The Kingdom of Spain*, SCC Case No. 2015/063; *Foresight Luxembourg Solar 1 S. Á.R.L., et al. v. Kingdom of Spain*, SCC Case No. 2015/150; See Happold, M. (2020). Belgium asks European Court of Justice to opine on the compatibility of Energy Charter Treaty’s investor-State arbitration provisions with EU law. EJIL Talk!

¹¹ Joined Cases C-798/18 and C-799/18, 29 October 2020, AG Opinion, footnote 55. Noteworthy, however, is that in this case the intra-EU setting was irrelevant, as the case is domestic. In an extra-EU setting, the CJEU might soon decide upon the compatibility of ECT Articles 1.6 and 26(1) with EU law. See CJEU, *République de Moldavie*, Case C-741/19.

Does Article 26 ECT apply to intra-EU disputes?

According to Belgium, the EU draft on the modernization of the ECT bears the risks that the dispute settlement mechanism “could be interpreted as allowing its application intra-European Union.”¹² In light of the ongoing legal struggle, this question is highly relevant, especially because the EU draft, published in April 2020, does not significantly change the wording of Article 26 of the ECT. The suggested text provides for investment arbitration and conciliation. It also adds the possibility for the contracting states to submit the dispute to the “the multilateral investment court.”¹³ The draft text also notes that nothing in the proposed revision has an impact on the EU’s goal of establishing a Multilateral Investment Court. More importantly, however, nothing in the draft touches upon the issue of intra-EU disputes, nor have the negotiations so far addressed the issue.¹⁴ This means that the draft provisions under Article 26 ECT have not been changed in their scope *ratione personae*.

The European Commission and the majority of EU member states support the view that the investor–state arbitration clause of the ECT, “if interpreted correctly,” would not be applicable between EU member states.¹⁵ More precisely, they argue that, by virtue of Article 26(6) ECT and Article 42(1) ICSID Convention, the Tribunal must determine its jurisdiction in accordance with the ECT and “applicable rules and principles of international law,” which would include EU law and the taking into account of the *Achmea* judgment. In this perspective, the ECT does not offer an invitation to arbitrate for investors in intra-EU constellations and in absence of an arbitration agreement, tribunals lack jurisdiction.

Conversely, post-*Achmea* ECT investment tribunals consider this question in a very different manner.¹⁶ In *Vattenfall v. Germany*, the tribunal held that Article 26(6), like Article 42(1) of the ICSID Convention, concerns

¹² Press release, *supra* note 2.

¹³ See EU draft of ECT, Art 26(3)(a), see also(4)(d), FN3.

¹⁴ Happold, *supra* note 10.

¹⁵ Communication from the Commission to the European Parliament and the Council, “Protection of intra-EU investment,” COM/2018/547 final. See Declaration, *supra* note 6.

¹⁶ E.g., *ESPF and others v. Italy*, ICSID Case No. ARB/16/5; *Eskosol v. Italy* ICSID Case No. ARB/15/50, *Masdar v Spain* ICSID Case No ARB/14/1.



only the law applicable to the merits of the dispute, and that otherwise nothing in Article 26 excludes intra-EU disputes from the scope of the provision.¹⁷ The tribunal added that even assuming that EU law was applicable for the purpose of determining its jurisdiction, the tribunal did not consider the CJEU's reasoning in *Achmea* to be applicable to intra-EU arbitration under an agreement to which the EU, as well as all member states, are party, such as the ECT and on which the CJEU has remained silent. Like other tribunals before, the *Vattenfall* tribunal also denies any conflict between Article 26 ECT and Articles 267, 344 TFEU, but remarks that even if such a conflict existed, EU law would not prevail over the ECT.

The arguments are subject to debate, and clarification from the CJEU is needed. Yet, the wording “the issues in dispute shall be decided in accordance with the provisions of this Treaty and rules and principles of international law” in Article 26 of the ECT points to the applicable law rather than the law applicable to the arbitration agreement. The same is true for Article 42(1) of the ICSID Convention. In the draft modernized ECT, the EU adds a footnote to Article 26(6) stating that “[f] or greater certainty, the domestic law of a Contracting Party shall not be part of the applicable law.” However, this footnote has no bearing on the determination of a tribunal's jurisdiction when accepting that the provision refers to the applicable law to the merits.¹⁸

Therefore, it appears that the draft text suggested by the EU cannot exclude that Article 26 of the ECT may be interpreted to apply in an intra-EU setting. This is notwithstanding the fact that under EU law, intra-EU investment arbitrations are incompatible with the EU Treaties and namely the autonomy of the EU legal order. As the CJEU will approach the issue from a purely EU law perspective, it will most likely decide the compatibility question in the negative.

Conclusion

If the CJEU finds the draft to be incompatible with the EU Treaties, the European Commission will have to remediate the content of Article 26 ECT and must subsequently convince the other ECT contracting parties. An opinion of incompatibility will also affect the roughly 40 pending intra-EU arbitrations under the ECT: in particular, the enforcement of such awards can then be challenged before domestic courts if enforcement is sought in EU member states.

Lastly, one should note that the treaty conflicts that exist between the current ECT and EU law are not only jurisdictional but also involve substantive conflicts given that the ECT is no longer in line with EU's objectives and IIAs practice. Questions arise about whether the draft text sufficiently reflects the EU's objective of climate change mitigation, as well as the ambitious Green Deal and energy-transition targets.¹⁹ On December 2, 2020, the European Commission confirmed for the first time that the EU could withdraw from the ECT “[i]f core EU objectives, including the alignment with the Paris Agreement, are not attained within a reasonable timeframe.”²⁰ While a collective withdrawal of all member states would also come with legal hurdles, we can conclude from the last developments that the future of the ECT has become increasingly uncertain.

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¹⁷ *Vattenfall v. Germany*, ICSID Case No. ARB/12/12, Decision on the Achmea Issue, 31 August 2018.

¹⁸ Adding this footnote is a consequence of current EU IIA practice, see CETA, Art 8.31 and CJEU, Opinion 1/17 *EU-Canada CET Agreement*, EU:C:2019:341.

¹⁹ On how these issues could be integrated see, Bernasconi-Osterwalder, N. & Brauch M.D. (2019). *Redesigning the Energy Charter Treaty to advance the low-carbon transition*. TDM. <https://www.iisd.org/publications/redesigning-energy-charter-treaty-advance-low-carbon-transition>

²⁰ Answer given by Executive Vice-President Dombrovskis on behalf of the EC. file:///Users/s3/Downloads/P-9-2020-005555-ASW_EN-2.pdf



NEWS IN BRIEF

Progress report on ECT modernization negotiations indicates familiar divisions among delegations as push for EU withdrawal grows

Following three negotiation rounds on ECT modernization last year, the most recent of which concluded on November 6, 2020, a leaked [progress report](#) from December 2020 suggests that state parties are still divided on key issues. This makes progress in negotiations, which require consensus from the national delegations, difficult to come by.

Likely complicating matters, these negotiations are taking place while high-profile cases are brought against EU member states by investors under the ECT. Most recently, the German company RWE has [initiated arbitration](#) against the Netherlands due to that country's coal phase-out. Other signs of EU member state discontent include Belgium's [request](#) that the CJEU issue an opinion on the ECT's compatibility with EU law and a recent [letter](#) from French officials expressing support for the possibility of withdrawal from the treaty.

The progress report documents ongoing discussions on a range of issues, from standard investment protection provisions such as FET and MFN, to the introduction of new clauses relating to CSR and sustainable development. The report also gives a glimpse of what could be considered two major factions—led by the EU and its member states on the one hand and Japan on the other—with significantly divergent views of the benefits and drawbacks of the ECT in its present form.

For its part, Japan is largely in favour of maintaining the status quo, while the EU and its member states, often accompanied by Georgia and Turkey, seek significant changes. For example, when it comes to standard provisions such as FET, MFN, and indirect expropriation, Japan appears to be in favour of upholding the current language. On the other hand, the EU and its member states, along with several others, favour more detailed definitions of these standards of protection, with, for example, the definition of FET including a closed list of violations. Similar tensions are clear in the parties' suggestions for changes to the MFN provision.

The EU and its member states, as well as Georgia and Turkey, are also pursuing stronger language on the right to regulate, CSR and sustainable development, and environmental protection. (*Editor's note:* we previously [reported](#) on the EU's proposal for ECT modernization, and much of the language from that proposal is now found in the recent progress report.) However, much of this is opposed by Japan, which remarked, with reference to the proposed curtailment of the indirect expropriation provision that “[p]roposals seem to be tilting the scales of balance overly to state concerns or right to regulate” and may “inappropriately undermine the level of investment protection to be achieved.”

The progress report provides details on how negotiations will move forward, noting that the COVID-19 pandemic slowed progress in 2020. The Chair has invited the group to hold four negotiation rounds in 2021 and also raised the possibility of informal meetings and workshops between negotiating rounds.

EU and China announce an “in principle” investment agreement

On December 30, 2020, after seven years of discussion, Brussels and Beijing announced the conclusion of the negotiations for an “in principle” Comprehensive Agreement on Investment (CAI) between China and the European Union. The [deal](#), the draft of which was released on January 22, was celebrated by the European Commission due to the Chinese commitment to granting a higher level of market access to EU investors, including opening new markets and ensuring fair treatment for EU companies operating in the country. Overall, the CAI is expected to create a better balance in EU-China trade, addressing asymmetries regarding European market openness, although there is [room for improvement](#) regarding its labour and environmental provisions.



According to the President of the [European Commission](#), the CAI is “an important landmark in our relationship with China and for our values-based trade agenda. It will provide unprecedented access to the Chinese market for European investors, enabling our businesses to grow and create jobs.” Ursula von der Leyen added that the deal “will also commit China to ambitious principles on sustainability, transparency, and non-discrimination. The Agreement will rebalance our economic relationship with China.”

The Europeans praised the CAI for the broader access of EU investments to the Chinese market, enabling competition on a more level playing field in China, including the country’s commitment to disciplining state-owned enterprises, transparency of subsidies, and rules against the forced transfer of technology. Key sectors of the European economy are expected to benefit from the agreement, such as manufacturing, including the production of electric cars, chemicals, telecoms, and health equipment. The Chinese government also committed to EU investment in numerous services sectors, such as cloud services, financial services, private health care, environmental services, and international maritime and air transportation.

As IISD [has observed](#), the EU’s high expectations are due in part to the “negative list” approach, which means that all sectors come under the purview of the agreement, except those specifically listed. Thus, experts [have argued](#) that the “negative list” demonstrates the Chinese “determination to promote a wider, broader, and deeper opening-up to the outside world.”

Nevertheless, as schedules and annexes to the agreement have not been released, it [may be](#) that China’s commitments do not go beyond domestic reforms such as the [Foreign Investment Law](#), which came into effect last year.

Sustainability and labour

Within CAI’s framework, Brussels and Beijing also agreed on sustainable development, environmental, and climate commitments, including the full implementation of the Paris Agreement and the prohibition of lowering environmental protection standards to attract investment. According to the European Commission, sustainable development issues will be subject to a strict enforcement mechanism by an independent panel of experts.

In addition, the agreement establishes that both parties should adopt corporate social responsibility (CSR)

and responsible business practices, as well as the ratification of ILO fundamental conventions, especially commitments on the ratification of the two conventions on [forced labour](#).

The implementation of all commitments outlined in the CAI will be monitored by the EU Executive Vice-President and the Chinese Vice-Premier. The text is now being translated and reviewed by both sides before being submitted to the respective parliaments. The EU and China are committed to finishing up the negotiations on investment protection and investor–state dispute settlement within two years after CAI’s signing.

French consortium kicks off an ICSID claim against Chile after USD 37 million loss due to COVID-19 pandemic

On January 19, 2021, the main shareholders of a consortium controlling the billion-dollar concession for Santiago’s Arturo Merino Benítez international airport informed Chilean President Sebastián Piñera of their intention to initiate an ICSID claim. The investors claimed they had suffered losses as a consequence of measures taken in response to the COVID-19 pandemic.

France’s Groupe ADP and Vinci Airports have 45% and 40% stakes respectively in the Nuevo Pudahuel consortium, which won a 20-year concession for Santiago’s airport in 2015, with the Italian company Astaldi holding the remaining 15%.

The French concessionaires’ claim under the 1992 [Chile–France BIT](#) demands compensation for net losses of USD 37 million in 2020, along with a contract renegotiation to prevent the expropriation of their investment. The consortium operators report that profits had fallen 90% in 2020, as Chile has lost 19



routes and 630 weekly frequencies since the pandemic broke out, which meant a drop of around 70% in passenger numbers.

The conflict escalated after the Chilean Ministry of Public Works refused the consortium's request for financial aid and an extension to the concession to restore its economic viability and recover the investment made in the new terminal currently under construction. Nuevo Pudahuel argued that the airport's revenue would be affected by the pandemic for at least the five-year period expected to return to previous passenger traffic levels.

According to the website *Pauta Bloomberg*, Minister of Public Works Alfredo Moreno alleged the state itself had also suffered considerable losses via the revenue-sharing mechanism that stipulates that 77% of the airport's profits should be handed over to the Chilean state. "For every peso that the concessionaire has lost, the state has lost three times as much," he added. Furthermore, it was argued that renegotiation is not permitted by law and would require a new public tender.

In the notice of dispute, the French operators mention Chilean government policy requiring additional sanitary measures to protect against the spread of COVID-19 at the airport, as well as the state's repeated refusal to renegotiate the contract. They also refer to the BIT's provisions on FET, national treatment, and protection against expropriation.

Speaking to *Pulso*, Groupe ADP CEO Fernando Echegaray pointed out that the refusal of the consortium's request posed serious risks to the concession, which would no longer be viable, as the contract does not assign the threat of pandemics to the consortium.

"The effects of the pandemic and the State's refusal to restore the economic-financial balance of the concession, however, have caused unexpected damage that not only will not allow greater investments but also put the airport's operation at risk. It is our opinion that Chile has not complied with its obligations to protect foreign investment under the agreement between the Government of the Republic of Chile and the Government of the Republic of France on the reciprocal promotion and protection of investments," said Echegaray.

Conversely, Minister Moreno noted that the airport is not at risk since the concessionaire can be replaced if Nuevo Pudahuel is unable to continue. "The companies have to comply with what has been asked of them, and

they cannot expect to use other mechanisms to receive what does not apply... what they are looking for is to extend the contract, which means billions," he said.

Looking at the ISDS claim under the Chile-France BIT, Rodrigo Yáñez, Chilean Undersecretary for International Economic Relations, emphasized that the divergence between the consortium and the Ministry of Public Works within the framework of the concession contract does not mean that the Chilean State is breaching its international obligations in the Chile-France investment protection agreement. "An eventual trial before the ICSID has the latter as its object and the recent award that put an end to the claim of the shareholders of *Alsacia and Express* against the State is very clear in distinguishing the actions of the State of a contractual nature and those carried out by the State in its sovereign capacity," explained Yáñez to *La Tercera*.

Before facing off with the Chilean State before the ICSID, the French controllers of Santiago's airport have begun a six-month amicable negotiation period imposed by Chile-France BIT.

UNCITRAL Working Group III: 40th session focused on elements of structural reform

The UNCITRAL Working Group III (WGIII) convened virtually from February 8 to 12 for its 40th session. During this session, the group's deliberations focused on two main issues related to structural reform of ISDS: the selection and appointment of ISDS tribunal members in the context of a "Standing mechanism" or "Standing body" (A/CN.9/WG.III/WP.203) and an appellate mechanism (A/CN.9/WG.III/WP.202).

Initially included in the agenda, the topics of enforcement and the code of conduct for adjudicators in ISDS (A/CN.9/WG.III/WP.201) were deferred to a future session by the WGIII due to lack of time.



The WGIII also agreed at the beginning of the session to remove the discussion on a [draft work and resourcing plan](#) from the agenda, and delegations were asked to submit written comments by March 1, 2021. IISD, CCSI, and IIED made a joint submission on the draft. The submission is the fourth in a [series of joint submissions](#) by the three organizations to the WGIII in the context of ISDS reform.

It was clarified during the session that comments and suggestions are made without prejudice to any delegations' final position on specific reform options; thus, deliberations do not imply any decision on the desirability and feasibility of a standing mechanism or an appellate mechanism.

As [observers](#) have noted, the chair of the working group has begun to push delegates toward finalizing a set of proposed reforms. However, for some delegates, it is premature to move to finalize a text, as there is insufficient agreement on the approach for structural reforms. Indeed, some delegations remain opposed to some proposed options, notably the permanent standing body and an appellate mechanism. On the other hand, other delegates appear eager to start developing and reviewing texts, including for a permanent body with a first instance and an appeal mechanism.

The discussions on the reform of ISDS Systems will resume officially in November. In the meantime, a series of intersessional meetings and informal sessions will be held on various topics aiming at preparing and advancing on topics that will be discussed at the next official sessions.

A webinar on the [draft Code of Conduct](#) was held on March 3, 4, and 8, 2021.

CETA Investment Court System advances toward implementation while Irish activists launch campaign opposing ratification

Four decisions adopted by Canada and the European Union on January 29 have moved the parties closer to implementing an Investment Court System (ICS) under the Canada-EU Comprehensive Economic and Trade Agreement (CETA). The decisions on appeals, interpretation, code of conduct, and mediation were formally endorsed by CETA's Joint Committee and Committee on Services and Investment (CSI) and will take effect once the dispute resolution provision of CETA comes into force.

Whereas CETA entered into provisional application in September 2017, most of its Chapter Eight, which includes the investor–state dispute resolution provisions, will be in force only when every EU Member State ratifies the agreement—so far, 15 out of 27 states have given notice of CETA ratification.

The decisions adopted on January 29 establish the [rules](#) for the Appellate Tribunal's functioning, including its composition and the procedures for modifying and reversing the ICS's legal findings and conclusions. The [rules for mediation](#), which aim at facilitating an amicable resolution of disputes, were also endorsed.

The adopted [Code of Conduct](#) for ICS judges establishes explicit disclosure, confidentiality, independence, and impartiality obligations, as well as prohibits former Tribunal or Appellate Tribunal members from acting as counsel before the Tribunal or Appellate Tribunal for three years from the end of their term. The fourth decision adopted sets out rules for [binding interpretations](#) by the CETA Joint Committee, ensuring that the provisions are interpreted as originally intended.

Ireland

Often described as a “second-generation” trade agreement, as it explicitly allows governments space to regulate in the public interest, CETA nevertheless faces increasing opposition from activists groups in Ireland, where Parliament postponed a vote to ratify the agreement last December after a huge public outcry. Among activists' concerns are the country's food sovereignty and impacts on small farmholders' long-term sustainability. The recently created Stop Ceta Ireland group launched a campaign against



CETA's ratification in February, which already achieved almost 1,500 followers on [Twitter](#).

For Attracta Uí Bhroin, from the [Irish Environmental Network](#), the ICS implementation could permit corporations to sue EU state members "for introducing progressive regulation." "It is absolutely critical for individuals who are concerned about not just the environment, but the impact on their back pocket and their tax bills, to get onto their local TD [Irish Members of Parliament] to express their concerns and say it hasn't been sufficient public debate," added her during an interview to [Action From Ireland \(Afri\) YouTube channel](#).



AWARDS AND DECISIONS

Kenya prevails in geothermal arbitration brought by WalAm Energy— ICSID tribunal rejects all claimant allegations

WalAm Energy LLC v. The Republic of Kenya (ICSID Case No. ARB/15/7)

Maria Bisila Torao

In an award dated July 10, 2020, an ICSID tribunal dismissed claims brought by WalAm Energy LCC (“WalAm”), a company incorporated in the United States and headquartered in Canada, over a geothermal project in the Republic of Kenya following Kenya’s removal of WalAm’s licence to explore and develop the Suswa geothermal concession. The tribunal found that Kenya validly removed WalAm’s licence by declaring it forfeited due to its failure to perform any physical work during a continuous period of six months.

Background and claims

In a July 20, 2007 letter addressed to the Minister of Energy, WalAm submitted an application for an authority to explore. Later, on September 5, 2007, WalAm Energy obtained a licence from Kenya’s Ministry of Energy, granting the entity exclusive rights to “enter, explore, drill for and extract, produce, utilize and dispose of geothermal steam and associated geothermal resources.” Separately, in a letter dated September 3, 2007, but signed by the minister on the same date as the licence, WalAm was given permission to explore for geothermal resources under Section 6(1) of the Geothermal Resources Act (the “GRA”).

In February 2009, WalAm informed the minister by letter that it had completed the exploration of the Suswa geothermal concession, along with prospecting and pre-feasibility analyses, and proposed to proceed with the geothermal licence rights and initial drilling. At that time, WalAm also asked the government to discuss the possibility of entering into a power purchase agreement (PPA) due to WalAm’s limited financial resources. Later in March, meetings between the government and WalAm representatives took place. Although Kenya engaged in preliminary discussions, a PPA was never concluded.

In March 2009, GeothermEx issued a feasibility report. However, WalAm did not provide a work program to the

government until February 2011. In March of that year, the work program was approved based on the understanding that the schedule would be strictly followed. By the end of the year, WalAm’s project had failed to progress and adhere to the program’s plan for that year.

On March 18, 2012, the government wrote a show cause letter stressing that WalAm was in breach of the licence as it had not carried out sufficient work at Suswa over the previous five years. The government also stated that “Under normal practice, it takes five years from geothermal resource exploration to construction of such power plants” (para. 284). On October 30, 2012, the Minister of Energy issued a forfeiture letter revoking WalAm’s licence. In response, WalAm filed for arbitration against Kenya under the licence dispute resolution clause, claiming a breach of customary international law for unlawfully declaring the licence forfeited and seeking hundreds of millions of dollars in compensation and reinstatement of the licence.

Domestic law is the applicable law. Customary international law may apply through domestic law

As the licence had no applicable law provision, WalAm argued that by consenting to arbitrate disputes “pursuant to” the ICSID Convention, Kenya agreed to arbitrate claims arising under Kenyan law and rules of international law because the tribunal’s jurisdiction is founded on the basis of Article 42(1) of the ICSID Convention and Kenyan law, which incorporates customary international law. This article provides that disputes in the absence of agreement between the parties on the applicable law should be decided “under the law of the Contracting State party to the dispute and such rules of international law as may be applicable” (Article 42(1) of the ICSID Convention). The claimant further submitted that Kenyan law and customary international law were applicable because Kenya had expressly incorporated international law into its Constitution. Kenya, however, argued that only domestic law was applicable because that was the law under which the licence was issued.

The tribunal upheld the respondent’s argument and reasoned that under Article 42 (1) of the Convention, Kenyan law was the applicable law because that was the State party’s law to the dispute and the law that applies to the legality of the licence. Also, the licence’s existence and validity derive from domestic law, as the government issued



it. The tribunal also added that customary international law could only be relevant when examining particular issues through local law because “customary international law is incorporated into Kenyan law [...], but that would not change the applicable law” for a particular issue. Customary international law would only apply to ancillary or general rules incorporated in Kenyan domestic law (para. 348).

Tribunal dismisses Kenya’s allegations regarding the validity of the licence

Kenya argued that under its domestic law, WalAm never applied for a licence because its letter dated July 20, 2007, was an application for authority only to explore. Consequently, a valid licence was never issued because the Minister of Energy never received a licence application. Therefore, the licence was *void ab initio* because the GRA requirements were not only a “mere formality” as claimed by WalAm (para. 361). The tribunal rejected Kenya’s arguments because the Ministry granted both despite WalAm’s application only for authority. Certainly, Kenya intended to grant both the authority to explore and the licence. The tribunal further stressed that despite the lack of clarity about the circumstances in which the minister’s licence came to be issued as the claimant only applied for an authority to explore, WalAm wished to obtain both authority to explore and a licence. Similarly, the minister intended to grant both and did so, considering that WalAm was compliant entirely with the GRA (para. 364).

Rightful declaration of forfeiture: Tribunal dismisses all grounds raised by the claimant

WalAm challenged the declaration’s validity on different grounds (on *ultra vires*; unjust enrichment; good faith; unreasonableness; proportionality; improper purpose; relevant and irrelevant considerations; procedural fairness; consent; estoppel, and reliance on own wrong). The tribunal rejected all allegations.

The government acted within its legal power

WalAm first argued that the government acted beyond its legal power (i.e., *ultra vires*) when it declared the forfeiture of the licence on the basis that WalAm had failed to build the power plant in five years. The tribunal, however, reasoned that contrary to what WalAm argued, the notice of forfeiture should only be interpreted in light of the licence and the GRA. Therefore, it concluded that the Minister of Energy was entitled to rely on Section 11(1)(a) of the GRA and the licence if no exploration activities were carried out for a continuous period of six months and expressly did so on the notice of forfeiture (paras. 412–428).

Failure to perform physical activity triggers the right to forfeit

WalAm also contended that the minister had no factual basis to rely on Section 11(1)(a) because the work WalAm had done before the forfeiture notice was served could be interpreted as work, considering work as any activity concerning the licence. To determine whether the claimant had carried out any work, the tribunal turned to the interpretation and meaning of the words “in or under the land” in the GRA, Section 11(1)(a), and “in or under the licence area” in the licence, clause 7(1)(a). The tribunal sided with the respondent’s interpretation that both expressions required physical activity (paras. 438–440). The tribunal further explained that this interpretation “reads the forfeiture provision in the context” and was therefore not narrow and literal as argued by WalAm but “consistent with the object and purpose of the licence” and the rights granted under it (para. 441).

Revocation of the licence was in good faith, reasonable and proportional

WalAm further argued that the licence’s revocation was in bad faith because the government’s ultimate goal was to transfer the licence rights to a public entity. The claimant further argued that the forfeiture was disproportionate and unreasonable under domestic law. The tribunal rejected these arguments on the basis that WalAm did not strictly adhere to the timetable. Moreover, given WalAm’s long history of inability to deliver since the work program’s approval on September 7, 2007, and to acquire sufficient financial resources to do so, the licence’s revocation was lawful and therefore reasonable and proportional.

No failure to take into account relevant considerations or consider irrelevant ones

WalAm further argued that the government failed to take into account “relevant considerations” when it decided to declare the licence forfeited. It is well established under Kenyan law that the exercise of discretionary public power may be found to have failed if “irrelevant considerations” are taken into account or “relevant considerations” are disregarded. The tribunal rejected this argument, indicating that as previously determined in its analysis, the reason for the forfeiture to be issued was that “no apparent efforts to explore and exploit the geothermal resources” had been made, and this was not an irrelevant consideration (para. 471). Similarly, the tribunal further concluded that Kenya had not failed to take into account any “relevant considerations.” The claimant’s belief that its obligations under the licence were suspended came from the expectations arising from its repeated statements that it needed a PPA to raise the funds that the infrastructure required to progress the project.



For the tribunal, such an assertion was illegitimate because the Minister of Energy expressly rejected a PPA on several occasions. First, it explicitly removed WalAm's reference to a PPA in its application when issuing the exploration licence. Secondly, when the 2011 work program was approved, government representatives did not adopt WalAm's timetable for a PPA. Therefore, according to the tribunal, the claimant's inability to raise sufficient capital resulted from the WalAm's deficiencies and its inadequacy (para. 493).

Consent and estoppel: Kenya's conduct could not have formed the basis of an estoppel or waiver as alleged by the claimant

WalAm further argued that Kenya consented in writing to the claimant not performing work in or under the land until it had a PPA or while negotiations for a PPA were ongoing and that Kenya should be estopped from relying on them to perform to trigger rights to forfeiture. The tribunal dismissed this claim because WalAm failed to prove that the government had expressly stated in any of its communications or letters that it had consented to the investor not performing work "in or under the land" until the conclusion of a PPA. No statement of consent or express representation could find estoppel to that effect. Moreover, the government informed WalAm of the minister's dissatisfaction with the lack of progress and work on many occasions. It was made clear in communications that the licence was under threat of forfeiture.

No legitimate expectations, as claimant failed to establish any evidential basis and support for its claim

The tribunal considered that the claimant could not argue that it had a legitimate expectation that it would not be required to begin drilling before a PPA was in place based on the government's conduct. Accordingly, it concluded that WalAm did not "have a legitimate expectation in the public law sense" as it failed to show that "statements were made by or on behalf of the government inducing such reasonable expectation" (para. 527)

Customary international law application: No breach of the minimum standard of treatment

WalAm invoked breaches of the customary international law minimum standard of treatment, arguing that Kenya had violated its duty to accord the claimant the minimum standard under Article 47 of the Kenyan Constitution and customary international law. According to the claimant, the government's obstructive conduct and refusal to act in good faith to negotiate a PPA prevented WalAm from moving forward and bringing the project into production.

The tribunal noted that all elements put forward by WalAm capable of constituting unfair treatment in breach of the international law standard have been previously considered in the tribunal's analysis and rejected. The tribunal added that expropriation did not apply, and any claims on the merits would have failed. Also, the tribunal concluded that even if the absence of objections or silence from the government can in some instances generate legitimate expectations (see *Gold reserve v. Venezuela*),¹ it could not give rise, in this particular case, to any expectations in relation to the conclusion or failure to obtain a PPA in the investment treaty context (paras. 558–561).

Costs

The respondent argued that all expenses should be borne by WalAm. Further, it added that even if the claimant were to prevail on liability, there should be an apportionment of costs to reflect the unnecessary costs caused by the claimant's conduct. In turn, the claimant argued that the respondent should bear the total arbitration costs incurred by the claimant.

The tribunal stated that the ICSID Convention "gives the widest discretion to allocate all costs of the arbitration" and noted that the respondent's legal costs were significantly lower than the claimant's costs.

Tribunal ordered WalAm to pay the respondent USD 648,857.75 for the respondent's portion of the arbitration costs and the sums of EUR 3,586,039.28 and USD 252,262.82 to cover 75% of the respondent's legal fees and expenses.

Notes: The tribunal was composed of Joe Smouha (president, nominated by the parties, British national), Swithin J. Munyantwali (claimant's appointee, British and Ugandan national) and James Spigelman (respondent's appointee, Australian national). The award of July 10, 2020, is available at <https://www.iareporter.com/articles/revealed-award-in-dispute-over-kenyan-geothermal-energy-project-comes-to-light/>

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¹ *Gold Reserve Inc. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB(AF)/09/1



UNCITRAL tribunal finds India in breach of India–UK BIT in proceedings brought by Cairn entities

Cairn v. India Cairn Energy PLC and Cairn UK Holdings Limited v. The Republic of India, PCA Case No. 2016-7

Trishna Menon

A PCA tribunal dismissed India’s jurisdictional objections and found it in breach of the FET standard in the India–UK BIT in an arbitration under UNCITRAL rules initiated by Cairn Energy PLC (Cairn Energy) and Cairn UK Holdings Limited (CUHL) (together, Cairn). The award was rendered on December 21, 2020.

Background and claims

The main subject of the claims was a series of transactions that took place among the Cairn group in 2006 (2006 Transactions), which reorganized the group’s Indian assets. As part of these transactions, Cairn Energy consolidated all the group’s Indian assets in 9 UK subsidiaries (9 Subsidiaries) and then incorporated CUHL in the UK and transferred its shares in the 9 Subsidiaries to CUHL, in consideration for CUHL shares. CUHL then incorporated Cairn India Holdings Limited (CIHL) in Jersey and transferred its shares in the 9 Subsidiaries to CIHL, in consideration for CIHL shares. The final step in the reorganization was the transfer of all of the Indian assets of the Cairn group to Cairn India Limited (CIL), the Indian subsidiary, by transferring CIHL from CUHL to CIL in a series of incremental stages (CIHL Acquisition).

Section 9(1)(i) of India’s Income Tax Act, 1961 (ITA), which was at issue in the dispute, according to Cairn, did not tax indirect transfers of capital assets situated in India. However, a year later, India’s Income Tax Department (ITD) attempted to change the settled interpretation of Section 9(1)(i) by seeking to impose capital gains tax on an indirect transfer by a non-resident in the Hutchison–Vodafone transaction. This attempt to “reinterpret” Section 9(1)(i) was rejected by the Supreme Court, in January 2012, in *Vodafone International Holdings BV v. Union of India & Anr. (Vodafone)*. A few months later, the Indian Parliament enacted an amendment to Section 9(1)(i) (2012 Amendment), which effectively overturned *Vodafone*, and amended Section 9(1)(i), according to Cairn, with retroactive effect, to cover indirect transfers by non-residents.

In 2014, the ITD notified CUHL that it had failed to report capital gains taxable in India arising from

the CIHL Acquisition and issued an order attaching CUHL’s equity shares in CIL, followed by an assessment procedure that culminated with a Final Assessment Order (FAO) in January 2016, and a Notice of Demand for capital gains tax of USD 1.6 billion, which, along with interest and penalties, amounted to approximately USD 4.4 billion (as of the date of Cairn’s claim). Cairn claimed that, since then, India forcibly sold approximately 99% of CUHL’s shares in CIL, and refused to allow CIL to distribute dividends to CUHL.

Cairn initiated arbitration, claiming that a series of measures imposed by India in relation to the 2006 transactions breached India’s obligations under the India–UK BIT, and sought full compensation for the losses flowing from those breaches. Specifically, Cairn claimed that India (i) failed to “create favourable conditions” for its investment and to accord Cairn and its investment FET, (ii) failed to accord its investments FET in violation of Article 3(2) of the BIT, (iii) unlawfully expropriated CUHL’s investment in CIL without providing fair and equitable compensation, and subjected Cairn’s investment to measures having an effect equivalent to expropriation, and (iv) violated Cairn’s right under Article 7 of the BIT to “the unrestricted transfer of their investments and returns” by depriving CUHL of the ability to sell its remaining CIL shares and to repatriate the proceeds, as well as the dividends that accrued in respect of these shares.

Tribunal dismisses India’s objections to jurisdiction and admissibility

India raised a number of objections to the tribunal’s jurisdiction, which were dismissed. India argued that Cairn’s Indian assets did not qualify as an “investment” under the BIT, firstly, because CUHL’s purported investment was not made in accordance with Indian law since the 2006 transactions were an abusive tax-avoidance scheme in violation of then-applicable laws. India did not dispute the fact that Cairn Energy made an investment in India in 1996 by acquiring an Australian company that held interests in a 1994 production-sharing contract in an Indian oil and gas field and subsequently various other assets, including production-sharing contracts and joint operating agreements. India did not allege that any of these acquisitive transactions were unlawful. The tribunal held that this arbitration related to this lawful investment, and this finding sufficed to conclude that the dispute fell within the tribunal’s jurisdiction.

The tribunal rejected India’s argument that the investment be considered in parts, with CUHL only acquiring its assets during the 2006



transactions, in accordance with the principle that jurisdictional inquiry as to whether a dispute relates to an investment should proceed by looking at the investment as a whole. Since Cairn's claims related to Cairn Energy's original investment, which has merely changed form over time, these claims fell within the tribunal's subject-matter jurisdiction.

Secondly, India contended that the BIT's definition of investment in Article 1(b) did not include indirect investments, and, as such, Cairn Energy's assets in India were not protected under the BIT. India relied on Article 5(3), which guaranteed compensation for expropriation for the shareholders of the expropriated company, arguing that this provision would be rendered superfluous if indirect investments were in any event protected under the BIT, and relied on *RosInvest v. Russia* which considered a similar provision. The tribunal, however, explained that the *RosInvest* tribunal did not suggest that the presence of such a provision in a BIT negated the existing right for shareholders to claim for their indirect loss and concluded that the context of the BIT, as reflected in its other provisions, did not suggest excluding indirect investments from its scope of application.

India made several additional jurisdictional objections. These included that Cairn's claims fell outside the scope of the tribunal's jurisdiction under BIT Article 9 because it concerned "returns" and not "investments," (ii) tax disputes could not be resolved by arbitration under the BIT due to an implied exception to its scope of application, and due to the fact that India and the UK have specifically agreed that tax disputes should be settled in accordance with the procedure prescribed in contemporaneous double taxation avoidance agreements. India also contended that taxation disputes were not arbitrable, either as a matter of international public policy, Indian law, or Dutch law (as the seat of the arbitration was the Hague). These arguments were also dismissed by the tribunal.

Violation of the FET standard found; other claims dismissed

Cairn argued that India's fiscal measures amounted to treatment that was unfair and inequitable under the BIT. The tribunal concluded that the tax assessment was based exclusively on Section 9(1)(i) of the ITA, as modified by the 2012 Amendment. With respect to the effect of the 2012 Amendment, the tribunal stated that the fact that Parliament labelled the amendment of Section 9(1)(i) a "clarification" was not dispositive of the international legal effect of the amendment. The

tribunal also concluded, based on its consideration of a wide range of evidence, that the 2012 Amendment substantively changed the scope or operation of Section 9(1)(i) and was thus not a true clarification, as India had argued. The 2012 Amendment purported to amend the content of Section 9(1)(i) from the date of enactment of the ITA (i.e., April 1, 1962). The mere fact that tax authorities were, in practice, precluded from levying taxes beyond the limitation period of six years did not change the period of retroactivity for which the 2012 Amendment purported to apply.

India argued that the 2006 transactions would have been taxable even without the 2012 Amendment because they were tax-avoidant transactions and were therefore taxable under the "look at" doctrine developed by Indian courts which focused on "substance over form." India also argued that the 2006 transactions were taxable irrespective of the 2012 Amendment because they involved the indirect transfer of immovable property and as such were taxable under Section 2(47)(vi) of the ITA. However, the tribunal found that India had failed to establish both these defences.

After this, the tribunal considered the question of whether retroactive taxation breached the FET standard. The tribunal stated that it would carry out a balancing exercise between India's public policy objectives and Cairn's interest in benefiting from the values of legal certainty and predictability. In order to achieve this balance, the specific reasons given to justify the retroactive application of tax measures would be assessed. Because India did not have a specific public purpose to justify applying the 2012 Amendment to past transactions, retroactive application of the 2012 amendment to the CIHL Acquisition failed to adequately balance Cairn's protected interest in legal certainty and India's power to regulate. By retroactively applying a new tax burden on a transaction that was not taxable at the time it was carried out, Cairn was deprived of their ability to consider the legal consequences of their conduct, violating the principle of legal certainty, which, according to the tribunal, was one of the core elements of the FET standard. Consequently, the tribunal concluded that India breached the FET standard in the BIT.

The tribunal decided that it did not need to address Cairn's remaining claims related to BIT Articles 3(1), 5, and 7. Since Cairn had requested the same reliefs for all these claims, even if the tribunal were to find merit in these claims, this would not affect its assessment of the appropriate reparation.



Reparation

Having found that India breached the FET standard in the BIT, the tribunal stated that it must then award relief that would “wipe out” the consequences of India’s breach of the BIT and place Cairn in the position it would have been had that breach not been committed. This would involve comparing what happened in reality with the situation which would, in all probability, have existed if that act had not been committed (But-For Scenario). The difference between both would be the measure of Cairn’s damages. Being satisfied that its jurisdiction to resolve the present dispute included the power to order India, as a measure of restitution, to withdraw its internationally unlawful tax demand, the tribunal declared that the tax demand against Cairn as set forth in the FAO was inconsistent with the BIT, and Cairn was relieved from any obligation to pay it. The tribunal also ordered India to withdraw the FAO permanently and refrain from seeking to recover the alleged tax liability or any interest and/or penalties arising from it.

The tribunal also allowed Cairn’s claim for compensation for the value of the CIL shares that India seized and sold in enforcement of its unlawful tax demand under the FAO. Cairn was awarded compensation for the value of the CIL shares at the amount of net proceeds that Cairn would have received from the sale of CIL shares in the But-For Scenario. Cairn also claimed compensation for corporation tax that they would allegedly have to pay in the UK on the amount awarded by the tribunal, at the 19% corporate rate, but the tribunal found that it had not established with a sufficient degree of certainty that it was likely to incur the UK corporation tax on the totality of the amount awarded for the proceeds of the CIL shares. Consequently, it dismissed this claim.

Decision and costs

The tribunal held that it had jurisdiction over the dispute and that Cairn’s claims were admissible. The tribunal found that India had failed to uphold its obligations under the UK–India BIT and international law, in particular, that it breached the FET standard under BIT Article 3(2). It made no declaration on any of the other issues in respect of which Cairn had requested relief.

India was directed to compensate Cairn for the total harm suffered by Cairn as a result of its breaches of the treaty, by an amount of approximately USD

1,232,820,143 along with interest at a rate of USD 6-month LIBOR plus a 6-month margin of 1.375%, compounded semi-annually. The tribunal also directed India to pay around USD 22,395,114 toward Cairn’s costs of arbitration and legal representation.

Note: The tribunal was composed of Laurent Lévy (president, Brazilian and Swiss national), Stanimir A. Alexandrov (claimant’s appointee, Bulgarian national) and J. Christopher Thomas QC (respondent’s appointee, Canadian national). The award is available at <https://www.iareporter.com/articles/a-1-2-billion-dollar-loss-for-india-as-cairn-energy-prevails-in-new-investment-treaty-award/>.

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