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Research Report

Investors' obligations under IIAs: Toward a practical solution

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Investors' obligations under IIAs: toward a practical solution

by

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A key feature of international investment agreements (IIAs) is their investor-state dispute settlement (ISDS) mechanism. As ISDS has been successfully utilized by foreign investors, some of the public's opinion of this mechanism has soured and resulted in something of a legitimacy crisis. This is caused, in part, by the asymmetric nature of IIAs whereby home and host states agree on each other's obligation to protect their respective investors—while the investors, as third parties to these agreements, undertake few, if any, obligations.

States have put more emphasis on policy and their right to regulate, as reflected in recent IIAs. Moreover, [UNCITRAL's Working Group III](#) has been working to improve ISDS procedurally. Although these efforts address the legitimacy crisis to some extent, they do not directly tackle the asymmetry in IIAs. To do so requires the imposition and enforcement of obligations against investors, to rectify the imbalance.

What kinds of obligation can be imposed on investors under IIAs? Most common are provisions on compliance with domestic laws and regulations and those related to corporate social responsibility (CSR), responsible business conduct (RBC) and human rights. Provisions on compliance with domestic laws and regulations are often found in the preamble or a stand-alone provision in IIAs; this approach is generally acceptable and linked to the [“clean hands” principle](#). On the other hand, provisions related to CSR, RBC or human rights, if they exist, are most commonly formulated in the form of “best effort” clauses that usually provide that investors “should” or “shall endeavor” to promote such concepts. How these “soft” obligations are enforced through ISDS is unclear.

Both kinds of obligations can be enforced through three methods. The first is to link investors' access to arbitration to their compliance with legal rules and standards, whether in domestic or international law. The second and third methods allow countries and affected individuals to enforce legal rules and standards [directly against investors through arbitration](#).

The latter two methods require a significant reimagining of the current ISDS legal infrastructure—which is not plausible anytime soon: even with regard to states, the [1969 Vienna Convention on the Law of Treaties](#) provides limited scope for imposing obligations on a third state. Accordingly, it would be much more complex to directly enforce an IIA obligation through arbitration against third-party investors, whose legal standing under international law is at best problematic, and whose consent to arbitration is not necessarily guaranteed. By contrast, the first method is more practical and readily implementable under the current system.

As the main beneficiaries, investors are granted the right to initiate ISDS proceedings under IIAs, although they did not negotiate the provisions therein. This feature is rather unique to IIAs. Setting conditions that must be met by investors before they can access arbitration aligns with this unique feature, and investors would have the incentive to comply.

In fact, similar conditions already exist in IIAs. For example, [Article 9.21 of the CPTPP](#) requires investors to give consent in writing to arbitration in accordance with the procedures set out therein and to include certain information in notices of arbitration. Failing to do so would render arbitration inaccessible. Consequently, an IIA obligation to comply with domestic laws and regulations, such as those on environment and anti-corruption, can be implemented in the same manner, albeit involving potentially more complex and lengthy proceedings to verify compliance. In addition, states could explicitly include a provision that obligates ISDS tribunals to take into account non-compliance with such an obligation when calculating damages, something akin to contributory fault.

Where domestic laws and regulations of host states are clear on investors' obligations, it is simpler to enforce compliance as a prerequisite to arbitration under IIAs since the corresponding IIA obligations can be linked to them, through the first method discussed above. However, where an IIA obligation only makes references to CSR, RBC or human rights more generally, or only in international law, investors will find it more difficult to comply and ISDS tribunals may not be willing to enforce the obligation. Consequently, states should incorporate—and elaborate—these concepts into their respective domestic legal systems vis-à-vis investors and their investments, to give a stronger legal basis for when IIA provisions refer, and link them, to investors' access to arbitration. For example, states could make it compulsory under their legal systems for foreign companies investing in mining projects to comply with human rights legislation or human rights conventions to which they are a party.

Until the time when it is widely acceptable to directly enforce IIA obligations against investors through arbitration, linking arbitration access to compliance with investors' obligations is the most practical way to deal with the asymmetry in IIAs.

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