THE ROLE OF TRANSNATIONAL SELF-REGULATED NORMS IN ADVANCING ENVIRONMENTAL ACCOUNTABILITY OF FOREIGN INVESTORS IN INVESTOR-STATE DISPUTE SETTLEMENT TRIBUNALS

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Abstract

This dissertation aims at mitigating the critical tension between promoting Foreign Direct Investment (FDI) as a financing mechanism for the *2030 Agenda for Sustainable Development* and the frequent neglect of environmental protection within the investor-state dispute settlement (ISDS) system. While International Investment Agreements (IIAs) and the ISDS tribunals they create are meant to facilitate foreign investment flow, this framework has historically favored investor protections over a host State's right to regulate environmentally. This has created an imbalance where foreign investors enjoy protective rights but have limited corresponding international environmental obligations. The dissertation's main goal is to propose a legally sound path for holding foreign investors environmentally accountable within the current ISDS framework, asking if transnational self-regulatory norms can be used as substantive law to impose international environmental obligations on investors during investment disputes.

Through doctrinal and theoretical analysis, it proposes using the systemic interpretation approach found in Article 31(3)(c) of the Vienna Convention on the Law of Treaties to determine if a transnational norm qualifies as a relevant and applicable rule of transnationalized customary international law for interpreting an investment treaty. To make this practical, the research uses the United Nations Global Compact (UNGC) as a case study, showing how it can be invoked as substantive law to hold investors accountable for environmental damage and confirming that a doctrinally and theoretically solid path exists for integrating investor obligations into investment arbitration.

Ultimately, the dissertation concludes that by treating qualified transnational self-regulatory norms as substantive law, ISDS tribunals can achieve a meaningful balance between investor rights and responsibilities, transforming investment arbitration from an impeding setting into a tool for fostering environmentally responsible investment and helping to achieve the goals of the *2030 Agenda for Sustainable Development*. This research is especially timely, as its arguments align with recent developments like the International Court of Justice's Advisory Opinion on climate change litigation, which underscores the urgent need to integrate environmental norms into international law.

Dedication

To my mom and dad, whose sacrifice of the joy of having me close has been the greatest gift to my success.

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It would not have been possible for me to complete this dissertation, a work of which I am immensely proud, without the guidance and unconditional support of my doctoral supervisor, Professor Craig Scott, whose insights and mentorship will continue to resonate throughout my scholarship for as long as I have the privilege to think and write. His sincere interest in my work has been a profound motivation for me to conduct my research with dedication and purpose, and I am constantly inspired by the depth of his intellect. Professor Scott's contribution extended far beyond intellectual guidance: he consistently showed genuine concern for the personal challenges I faced, as well as for the difficulties unfolding back home—from parenting responsibilities to the tragic war. I am deeply grateful—and profoundly joyful—to have had the opportunity to learn from and work alongside him. I sincerely hope that the years of our PhD journey together mark not an ending, but the beginning of many future collaborations.

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Introductory Roadmap

Foreign direct investment (FDI) serves as a pivotal financing mechanism for the *2030 Agenda for Sustainable Development* and its 17 Sustainable Development Goals (SDGs).[1] The potential of FDI in promoting sustainable development can be achieved through the implementation of regulatory frameworks that not only increase FDI flows but also prioritize FDI projects in critical sustainable development sectors. To increase FDI inflows, States engage in negotiations to establish international investment agreements (IIAs). IIAs are anticipated to facilitate FDI by granting foreign investors the right to receive protective investment treatment in host States. Furthermore, IIAs are crucial in establishing investor-state dispute settlement (ISDS) tribunals that hold host States accountable for any violations of investment-protection standards.

Developing countries have long considered IIAs as instrumental to their broader development strategy, particularly in enhancing their attractiveness to be destinations for FDI. FDI, as a source of external financing, promotes economic growth by injecting capital, creating employment, transferring technologies, and improving infrastructures. However, attracting FDI is highly competitive and risk-sensitive, especially with respect to developing countries that are perceived as having weak governance frameworks as they may lack robust legal systems and suffer from political instability. In this context, IIAs are seen as mechanisms that help mitigate these concerns and provide reassurance to foreign investors. By making commitments to investment protection and by offering the dispute resolution of ISDS tribunals, IIAs are developed to alleviate fears of arbitrary or discriminatory treatment by host States, thereby encouraging investment flows. State parties to IIAs send a signal to the international investment community that they are open for business and committed to protecting foreign investors. This signaling effect can have substantial reputational benefits, positioning the country as a credible and safe investment destination in a competitive global market.

However, the assumption that FDI inherently fosters sustainable development is oversimplified. Over the past several decades, numerous studies and civil society reports have warned that

[1] United Nations, *Transforming Our World: The 2030 Agenda for Sustainable Development* (2015), online: <https://docs.un.org/en/A/RES/70/1>.

investment-driven economic growth—especially when facilitated through IIAs lacking robust environmental safeguards—can exacerbate environmental harm. In particular, FDI in extractive industries or high-carbon sectors have been linked to widespread environmental degradation (including climate change induced by greenhouse gas emissions). These sectors often operate under weak regulatory frameworks in host States, especially in developing countries, where environmental governance may be undermined by limited institutional capacity or political pressure to attract foreign capital at any cost. In such circumstances, host States may resort to regulatory measures against foreign investments to safeguard the natural environment, thereby risking infringement of investment-protection standards included in IIAs.

This then leads to investor-state disputes between foreign investors making environmentally risky investments and host States taking environmentally protective measures in ISDS tribunals. In these cases, it falls to the human decision-makers acting in the name of ISDS tribunals to award in favor of either investment protection or environmental consideration. Despite the pressing importance for ISDS tribunals to be part of guiding FDI towards sustainable development, they often impede host States' regulatory power of environmental protection. ISDS tribunals' large monetary awards in favor of foreign investors play an impeding role, in the first place, by pressuring host States not to undertake environmental measures that they would otherwise be legally entitled to adopt. If they do proceed in the face of the risk of an adverse ISDS finding, then States have to compensate financial damage caused by their environmental measures when measures are found to violate the terms of IIAs—and also abandon those measures for the future, lest they be forced to pay compensation again.

While ISDS tribunals may appear to uphold the formal equality of States—given that their jurisdiction derives from freely negotiated treaties—they predominantly serve to protect foreign investors from developed countries. These investors benefit from a dispute resolution system grounded in IIAs that reflect and perpetuate historical global power imbalances. IIAs, as the central substantive international law in the dispute settlement process, do not strike a balance between the rights and obligations of disputing parties to the extent that host States are the primary entities responsible for safeguarding the economic rights of investors through ensuring a stable regulatory environment that promotes investment protection and economic growth. The

flipside is that foreign investors are the entities that enjoy protective rights without—in classical or mainstream doctrinal understandings—being internationally responsible to host States while being responsible under the national laws of host States only in highly circumscribed ways.

ISDS decisions ensuing from contests between investors' protective rights and environmental measures of host States are generally regarded as disfavoring SDGs—that is multiple and holistic goals going beyond the superficial investor-driven notion of investment having the potential to contribute to sustainable development by dint simply of economic activity and growth. This dynamic discloses the failure of ISDS tribunals to take into consideration foreign investors' environmental obligations and challenges the notion that FDI is unambiguously aligned with SDGs. A striking illustration of the climate change-related consequences of this dynamic is the growing reliance on ISDS tribunals by foreign fossil fuel investors to contest environmental measures implemented by host States, leveraging ISDS's investor-protective awards to resist host States' environmental regulatory actions.

To reorient FDI towards the *2030 Agenda for Sustainable Development*, I aim in this PhD dissertation to balance the rights and obligations of foreign investors in ISDS tribunals in order to have both investment and investment arbitration contribute to inclusive, environmentally responsible investment practices. This requires a distinctive solution whereby ISDS tribunals are able and willing to consider international environmental obligations of foreign investors and, consequently, engage in a balancing act between the competing priorities of investment protection and environmental considerations at the transnational level. With this objective in mind, I structure this research around this central question: *Could transnational self-regulated norms be invoked as liability law to impose international environmental obligations on foreign investors and then be treated as substantive law beyond the law of IIAs themselves in order to hold the investors environmentally accountable in investor-state disputes brough before ISDS tribunals?*

Bracketing the issues of whether the ISDS system ought to be changed structurally and how IIAs texts should be reformed substantively, I aim to find pathways for transnational self-regulated norms concerning environmental responsibilities of foreign investors be treated as part of the

substantive law governing the merits of investment disputes. This would improve arbitral decision-making from an environmental standpoint by opening doors to the meaningful consideration of foreign investors' environmental responsibilities such as those included in the United Nations Global Compact, as a matter of substantive law. By systematically involving transnational self-regulated norms in the investment dispute settlement process, ISDS could even be transformed into a window of opportunity for fostering more robust understandings of the relationship between investment and sustainable development according to which "foreign-investment and environmental protection have the possibility to move from being potentially conflicting to potentially supportive realities, and States have a chance to put environmental considerations on equal footing with trade and investment concerns."[2]

In relation to the doctrinal, theoretical, and practical objectives of this study, I will adopt a four-pronged research pathway. Each prong, corresponding to each of four main chapters (apart from this introductory roadmap and a brief concluding part on future directions), not only constitutes a contribution to the examination of specific legal aspects of transnational self-regulated norms as substantive law in ISDS tribunals but also cumulatively generate a major step towards achieving the *2030 Agenda for Sustainable Development*.

Chapter 1 serves as the foundational building block of this dissertation, conducting doctrinal analysis to establish the contextual and conceptual framework for the current functioning and limitations of ISDS tribunals. It begins by highlighting the critical role ISDS tribunals play in global investment governance and their influence over the policy space of host States seeking to implement environmental-protection measures. This chapter critically examines how ISDS tribunals, while originally designed to protect foreign investors, have increasingly become instruments through which regulatory efforts—particularly those aimed at environmental protection—are contested and, in some cases, effectively curtailed. Through detailed analysis, it discloses how the existing structure of ISDS disproportionately prioritizes investment protection, often at the expense of environmental considerations and the sovereign right of States to regulate in the public interest. It underscores the pressing need to reconsider the legal position of

[2] Ted Gleason, "Examining Host-State Counterclaims for Environmental Damage in Investor-State Dispute Settlement from Human Rights and Transnational Public Policy Perspectives" (2021) 21:3 International Environmental Agreements 427–444.

investors—not merely as rights-holders but as entities that may also bear enforceable obligations under international law. Chapter 1 culminates in a focused analysis of the *Urbaser v. Argentina (2016)* case, which serves as a key turning point in ISDS jurisprudence.[3] For the first time, an ISDS tribunal expressly acknowledged that foreign investors could, in principle, be subject to direct international obligations—in that case, obligations arising under the customary international law of human rights. This development, so far, has been limited in its own scope and has not had a significant impact on subsequent ISDS cases. Yet, it has very much opened a critical legal and conceptual door for considering similar obligations in relation to environmental protection—as evidenced by an already extensive scholarly literature discussing this one case and its implications. The *Urbaser* case is used as example to demonstrate how ISDS tribunals might evolve from institutions that merely enforce investor protections included in IIAs to ones that can also engage with international environmental norms imposing responsibilities on investors.

Chapter 2 constitutes the first integral step in examining the possibility of involving transnational self-regulated norms within investment dispute settlement procedures. It develops a principled framework for how ISDS tribunals determine the substantive law in investment disputes. At the outset, it clarifies that, while investment treaties provide the primary source of substantive law, international customary norms play a critical role in the treaty interpretation process. In order to address core interpretive challenges as to how, when, and to what extent tribunals may engage transnational self-regulated norms for investment treaty interpretation, this chapter delves into Article 31(3)(c) of the Vienna Convention on the Law of Treaties that notes "relevant rules of international law applicable in the relations between the parties" should be engaged in the treaty interpretation process.[4] To operationalize which customary norms—including those potentially embodied in transnational self-regulated norms—qualify as *relevant* rules of international in treaty interpretation, this chapter introduces and discusses in some detail a two-part framework for assessing relevance: sameness of subject-matter of investment treaty and customary law as well as consistency between rules of investment treaty and customary law. The

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[3] *Urbaser SA and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic*, ICSID Case No ARB/07/26, Award 8 December 2016.

[4] *Vienna Convention on the Law of Treaties, United Nations Treaty Series, 1155, 23 May 1969 (entered into force 27 January 1980)*.

chapter argues that this structured approach offers both flexibility and legal coherence and paves the way for tribunals to systematically assess the customary norms included in transnational self-regulated norms as relevant rules of international law that inform or influence the interpretation of investment treaty.

Chapter 3 is the second integral step to determine the role of transnational self-regulated norms in investment dispute settlement procedures. It evolves its discussion around the applicability requirement, included in the already quoted Article 31(3)(c) of the Vienna Convention on the Law of Treaties—namely, that portion that says "international law applicable in the relations between the parties" should be engaged in the treaty interpretation process. The central aim of this chapter is to discuss the institutional and normative dimensions of what I call "transnationalized customary international law"—inclusive of law reflected or generated by transnational self-regulated norms—as *applicable* international law that ISDS tribunals should not only consider but also actively apply when interpreting investment treaties. Treating transnationalized customary international law norms as applicable rules of international law in the treaty interpretation process involves the assessment of whether those rules are both opposable to and legally binding on foreign investors in order to hold them environmentally responsible at the transnational level. To support this argument, the chapter evaluates the lawmaking authority of transnational self-regulated norms as transnationalized customary international law through the lens of several theoretical approaches to international and transnational legal doctrine. There are first hybridity and pluralism theories, which provide a conceptual basis for understanding how non-state actors participate in the creation of transnational legal norms, particularly how such norms emerge from complex networks that transcend traditional state-centric legal frameworks. The chapter then turns to interactional theory that explains how transnationalized customary norms can be legitimized as law if they adhere to a set of "criteria of legality" and if their subjects, who have created them, reciprocally fulfill duties while developing a sense of obligation towards the norms.

Chapter 4 operationalizes the doctrinal and theoretical findings developed in the preceding chapters by applying them to a concrete case study. The United Nations Global Compact (UNGC) will be analyzed here as a paradigmatic transnational self-regulated norms—and one

entitled to the status of law.[5] This chapter marks a key transition from abstract theory to practical application, demonstrating how the normative framework developed in earlier chapters can guide ISDS tribunals in engaging transnational self-regulated norms imposing international responsibilities on investors in investment disputes. Before examining how and under what conditions the UNGC may have evolved into a relevant transnationalized customary international law applicable to foreign investors, this chapter establishes a further doctrinal foundation for how exactly an international law of obligations on investors can be applied in the context of an investment arbitration. The chapter provides an overview of the "post-establishment illegality defence," wherein the "illegality" referenced in the concept is that of conduct breaching international legal obligations directly owed by an investor—distinguishing this defence from investment law's understanding of loss of protection when an investor breaches of domestic-law conditions of establishment. Under the post-establishment illegality defence, host States counterpose harms caused by the environmentally risky conduct of foreign investors—treated as direct violations of international law by the investor—to the compensation demanded by those investors for alleged violations of investment-protection rights granted by IIAs. Using the plea of post-establishment illegality, host States may invoke the UNGC as substantive law in order to hold investors environmentally accountable in ISDS tribunals. By introducing this defence and explicating the legal character of the UNGC, the chapter examines the extent to which the UNGC is a viable pathway for striking a balance between the protective rights and environmental responsibilities of foreign investors. Chapter 4 reinforces the broader argument established in Chapters 2 and 3 on the role of rules of international law outside a treaty in the interpretation of that treaty: transnational self-regulated norms, if they meet the requirements of both relevance and applicability can be treated as substantive law to hold foreign investors environmentally accountable before ISDS tribunals. Ultimately, this chapter argues that, by interpreting the applicable law in investment treaty arbitrations as including the UNGC, ISDS tribunals will advance the realization of *the 2030 Agenda for Sustainable Development*, an objective central to this dissertation introduced and discussed in Chapter 1.

[5] United Nations Global Compact (UNGC), *The Ten Principles of the UN Global Compact*, online: <https://unglobalcompact.org/what-is-gc/mission/principles>.

I structure this dissertation in a way that each chapter leads reasonably to the next, with Chapter 4 serving as the substantive conclusion to the study. As such, there is no need for a formal concluding chapter that merely reiterates what has already been argued—and often recapped—throughout the previous chapters. Instead, I include a brief final part to the dissertation, in lieu of a "Conclusion," that is entitled "Concluding Pathways." This part shifts the focus forward, looking at the potential for the dissertation to lead to further research and writing that broaden and deepen specific themes or elements. It also positions the dissertation as a launching pad for future research inquiries. This final chapter reflects on unresolved questions, emerging issues, or theoretical insights that have surfaced during this research, but which fall outside the current scope of analysis. In this way, it highlights how the dissertation contributes to current academic debates and at the same time invites both me and other scholars to take up and expand upon these debates to be part of the ongoing conversation in the fields of international investment law, sustainable development, and transnational environmental governance.

Chapter 1: Investments and Sustainable Development: Friends or Foes?

1.1 Sustainable Development and Foreign Direct Investment

Foreign direct investment (FDI) is a principal means of financing the *2030 Agenda for Sustainable Development* and its 17 Sustainable Development Goals (SDGs). However, the potential contributions of FDI to sustainable development can be realized only by implementing regulatory frameworks that maximize FDI flows while prioritizing FDI projects in critical sustainable development sectors. To address the former point and enhance the investment climate for attracting FDI flows, States negotiate international investment agreements (IIAs). For developed and capital-exporting countries, IIAs are part of long-lasting efforts to establish international rules facilitating and protecting foreign investments by their nationals and companies. Developing countries have negotiated IIAs as part of their desire to improve their policy framework in order to attract more FDI and benefit from it. IIAs, therefore, are supposed to facilitate FDI by granting foreign investors specific standards of treatment and, most importantly, recourse to investor-state dispute settlement (ISDS) tribunals to allege the violation of these standards by host States.

However, not all investors would make FDI projects in critical sustainable development sectors. Instead, there are situations in which FDI projects are taking place in high-carbon and resource-intensive polluting sectors, placing additional burdens on the environment. And even "green economy" projects that focus on achieving some environmental benefit (for example, solar and biomass projects or mono-forestation sold as carbon sinks) have such massive negative impacts, for example, on biodiversity that it is difficult to characterize them as sustainable development projects. For decades, there have been warnings that this type of economic growth stimulated by investment agreements may harm social and environmental sustainability. In these situations, host States might take regulatory actions against foreign investments in order to protect the natural environment. This will lead to arbitral cases between foreign investors making the environmentally risky FDI projects and States hosting the environmentally risky FDI projects in

ISDS tribunals. In these cases, it falls to the human decision-makers acting in the name of ISDS tribunals to make decisions that manage the tensions between investment protection and environmental objectives.

In this situation, ISDS has been assumed to be a window of opportunity by means of which "foreign-investment and environmental protection have the possibility to move from being potentially conflicting to potentially supportive realities, and States have a chance to put environmental considerations on equal footing with trade and investment concerns."[6] Despite the pressing importance of ISDS tribunals, there remains comparatively little scholarly legal analysis on how the decision-making of such tribunals can affect a country's potential to meet its sustainable development goals and targets.[7] In this chapter, I intend to address this gap. I will focus my attention on the sustainable development aspects of the dispute settlement procedures offered in ISDS tribunals. I examine this central question: *To what extent could IIAs foster sustainable development in host States by means of FDI? Or, conversely, to what extent does the access to ISDS tribunals by foreign investors frustrate environmental protection and thus sustainable development?* Ultimately, I seek to understand the impeding role of ISDS tribunals concerning environmental protection and—in subsequent chapters—propose some possible reforms of imposing environmental obligations on foreign investors in cases before ISDS tribunals in order to strike a balance between competing priorities of investment protection and environmental consideration in investment law.

First, I begin the discussion with a brief explanation of the evolution of the concept of "sustainable development" and assumptions about the positive effect of IIAs on sustainable development by means of promoting FDI flows. Second, I direct the discussion towards the interaction between ISDS tribunal and sustainable development. In this section, I examine case

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[6] Gleason, *supra* note 2.

[7] Marie-Claire Cordonier Segger, *Crafting Trade and Investment Accords for Sustainable Development: Athena's Treaties* (Oxford University Press, 2021) is the most recent scholarly contribution on this topic. This book mostly focuses on the capacity of investment treaties to integrate sustainable development goals within their contexts. It goes beyond simple comparisons of environmental measures or human rights concerns in order to conduct an intensive analysis of how future trade and investment accords could actually be crafted to promote achievement of the world's SDGs.

law and scholarly commentary concerning the role of IIAs in sustainable development and then, more specifically, survey additional relevant scholarly documents, cases, and commentary on the structure and general criticisms associated with ISDS tribunals. In addition, after providing an overview of the general criticisms of ISDS tribunals, I narrow the domain of this research by focusing on the particular context of environmental dispute resolution in ISDS tribunals. I emphasize the impeding role of ISDS tribunals in considering environmental issues and, most notably, underline ways by which foreign investors use ISDS tribunals to threaten the regulatory power of host States toward environmental protection. Third, in light of the difficulties associated with legitimizing host States' regulatory measures taken under their environmental obligations, I provide the background context for this dissertation's proposal that focuses on foreign investors' international obligations rather than those of host States to steer FDI activities toward sustainable development. In the last section of this chapter, I conduct an in-depth analysis of the *Urbaser* case, decided by ISDS tribunal in 2016, to explain how doors could be open for ISDS tribunals to give environmental considerations commensurate importance in cases brought by foreign investors that come before them. I also consider how States may not only respond with counter-claims but also initiate claims before ISDS tribunals on the ground that foreign investors have breached their own direct international obligations.

1.1.1 The Evolution of Sustainable Development

The concept of "sustainable development" was discussed for the first time in 1987 in the *Report of the World Commission on Environment and Development: Our Common Future*, which was produced by the United Nations World Commission on Environment and Development (also known as the *Brundtland Commission*).[8] The report was a response to growing global concerns about the interplay between environmental sustainability, economic development, and social equity: many forms of development erode environmental resources, environmental degradation can undermine economic development,[9] and poverty is a significant cause and effect of global

[8] United Nations World Commission on Environment and Development, *Report of the World Commission on Environment and Development: Our Common Future* (1987), online: <https://digitallibrary.un.org/record/139811?ln=en&v=pdf>.

[9] The United Nations Economic and Social Commission for Western Asia defines environmental degradation as "the deterioration of the environment through depletion of resources such as air, water and soil; the destruction of ecosystems and the extinction of wildlife. It is defined as any change or disturbance to the environment perceived to be deleterious or undesirable." Environmental degradation could thus be summarized as the triple planetary crisis of climate change, pollution, and biodiversity loss, United Nations Economic and Social Commission for Western Asia,

environmental problems. It noted that critical global environmental problems are the outcomes of the massive poverty in the South and the non-sustainable patterns of consumption/production in the North. The report then called for a new strategy that aligned economic development with environmental protection—encapsulated by the now-common term of sustainable development. *Our Common Future* significantly impacted global policymaking and set the stage for subsequent international agreements and conferences on sustainable development as a new way of decision-making that seeks to not restrict economic growth in developing countries while sustaining human progress and ecological survival for the entire planet into the distant future. The report continues to be a seminal document in sustainable development discourse, highlighting the urgent need for collective action and long-term thinking to ensure a sustainable and prosperous future for all. It provides a descriptive definition of sustainable development:

> Humanity has the ability to make development sustainable to ensure that it meets the needs of the present without compromising the ability of future generations to meet their own needs. The concept of sustainable development does imply limits -- not absolute limits but limitations imposed by the present state of technology and social organization on environmental resources and by the ability of the biosphere to absorb the effects of human activities. However, technology and social organization can be both managed and improved to make way for a new era of economic growth. The Commission believes that widespread poverty is no longer inevitable. Poverty is not only an evil in itself, but sustainable development requires meeting the basic needs of all and extending to all the opportunity to fulfill their aspirations for a better life. A world in which poverty is endemic will always be prone to ecological and other catastrophes.[10]

This definition of sustainable development shaped the foundation of the United Nations Conference on Environment and Development, held in Rio de Janeiro in 1992. The Conference proposed the *Agenda for Environment and Development*, also known as *Agenda 21*,[11] as well as the *Rio Declaration*,[12] to draw up action plans and strategies for moving towards a more sustainable pattern of development. *Agenda 21* is a comprehensive action plan for sustainable

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"Environmental Degradation" (2015), online: *United Nations Economic and Social Commission for Western Asia* <https://archive.unescwa.org/environmental-degradation>.

[10] United Nations World Commission on Environment and Development, *supra* note 8 para 27.

[11] United Nations Conference on Environment and Development (UNCED), *Agenda for Environment and Development, Agenda 21* (1992), online: <https://sustainabledevelopment.un.org/content/documents/Agenda21.pdf>.

[12] United Nations Conference on Environment and Development (UNCED), *Rio Declaration on Environment and Development* (1992), online: <https://www.un.org/en/development/desa/population/migration/generalassembly/docs/globalcompact/A_CONF.151_26_Vol.I_Declaration.pdf>.

development that provides a blueprint for addressing social, economic, and environmental challenges at the global, national, and local levels. It outlines strategies and recommendations for achieving sustainable development across various sectors, including poverty eradication, sustainable consumption and production, biodiversity conservation, and stakeholders' roles in implementing sustainable development practices. The *Rio Declaration*, on the other hand, is a more general document, consisting of a set of 27 principles that establish States' fundamental rights and responsibilities in promoting sustainable development. It emphasizes the importance of environmental protection, equity, and the participation of all stakeholders in decision-making processes.

The *Rio Declaration* and *Agenda 21* are interconnected and mutually reinforcing. The *Rio Declaration* provides a guiding framework for sustainable development principles and values, while *Agenda 21* offers a practical roadmap for implementing those principles and achieving sustainable development goals. Together, they seek to provide a comprehensive approach to addressing environmental conservation and socio-economic development challenges. Both the *Rio Declaration* and *Agenda 21* have had a significant impact on shaping global sustainable development policies and practices. They remain essential references for policymakers, governments, and organizations working towards a more sustainable and inclusive future.

The pressing need to ensure cooperation for sustainable development and advance environmental, social, and economic priorities in an integrated manner is clearly reflected in the consensus of over 190 States in the 2002 World Summit on Sustainable Development. That World Summit, held in Johannesburg, was a significant milestone in advancing the global agenda for sustainable development. The Summit aimed to build upon the outcomes of the Rio de Janeiro conference and address new challenges and opportunities that had arisen since Rio. The 2002 World Summit focused on key thematic areas such as poverty eradication, water and sanitation, energy, health, biodiversity, agriculture, and sustainable consumption and production. It aimed to promote the integration of economic, social, and environmental dimensions of sustainable development and foster partnerships among governments, international organizations, civil society, and the private sector. The Summit resulted in the adoption of the *Johannesburg Declaration on Sustainable Development* and *the Plan of Implementation* to guide governments, organizations, and

stakeholders in their efforts to promote sustainable development, address environmental challenges, and achieve social and economic progress in a balanced and integrated manner.[13] The *Johannesburg Declaration on Sustainable Development* emphasized the need to integrate economic, social, and environmental aspects in decision-making processes in order to achieve sustainable development. It also recognized poverty eradication as a central objective and emphasized the need to address the needs of the poorest and most vulnerable populations via strengthening partnerships among governments, civil society, and the private sector to promote sustainable development. The *Plan of Implementation* likewise provided a roadmap for translating the commitments made in the *Johannesburg Declaration* into concrete actions. It addressed various thematic areas and identified specific targets, actions, and mechanisms for implementation. It mostly called for the promotion of sustainable consumption and production patterns, trade, and investment to minimize resource depletion, waste generation, and pollution.

In 2012, the United Nations Conference on Sustainable Development was held in Rio de Janeiro and was another landmark event in the field of sustainable development, following the landmark conference in the same city twenty years before. It aimed to assess progress, gaps, and new challenges to secure renewed political commitment to sustainable development. The conference resulted in the adoption of a key document called *The Future We Want*.[14] *The Future We Want* reaffirmed political commitments to sustainable development and outlined a vision for the future. It emphasized the importance of poverty eradication, sustainable development goals, and the integration of economic, social, and environmental dimensions to promote a balanced and integrated approach. The document highlighted the potential of green technologies, renewable energy, sustainable agriculture, and resource efficiency in promoting sustainable development. The *Future We Want* document emphasized the importance of providing adequate means of implementation for sustainable development, particularly for developing countries, via financial resources, technology transfer, capacity-building, and partnerships that support sustainable development efforts.

[13] World Summit on Sustainable Development (WSSD), *Johannesburg Declaration on Sustainable Development and the Plan of Implementation* (2002).
[14] United Nations Conference on Sustainable Development, *The Future We Want* (2012), online: <https://sustainabledevelopment.un.org/futurewewant.html>.

All these initiatives have influenced the subsequent global framework on SDGs. In 2015, the *2030 Agenda for Sustainable Development* became the most recent global blueprint for addressing the pressing social, economic, and environmental challenges facing our world. It was adopted by all United Nations member States and consists of 17 SDGs divided into 169 targets to be achieved by the year 2030.[15] The 17 SDGs encompass a wide range of interconnected issues, aiming to create a more sustainable and equitable world. Each goal addresses a specific area of concern, including poverty eradication, quality education, clean energy, gender equality, sustainable cities and communities, responsible consumption and production, climate action, and biodiversity conservation. The SDGs recognize that sustainable development requires holistically addressing economic, social, and environmental dimensions.

The interconnectedness of the goals reflects the fact that progress in one area is closely linked to progress in others. The *Agenda* also states that SDGs should be adopted by all countries, regardless of their level of development, and call for global cooperation and partnerships. Such goals emphasize the shared responsibility of all nations in achieving sustainable development and highlight the need for collaboration among governments, civil society, businesses, and other stakeholders. The SDGs aim to bring about transformative change by setting ambitious targets that go beyond business as usual. They call for innovative approaches, policy reforms, and sustainable practices to address systemic issues and create long-term positive impacts. The SDGs prioritize reaching the most vulnerable and marginalized populations, ensuring inclusive and equitable progress. Since 2015, the *2030 Agenda* has gained significant traction globally and has become a standard reference point for governments, organizations (including universities like York), and individuals working towards sustainable development. It provides a shared vision and a roadmap for action, guiding policies, investments, and initiatives at all levels to create a more sustainable and prosperous future for all.

This evolutionary path discloses that the interrelationship between the environment, economy, and society has been identified as the integrating (and integral) dynamic of sustainable development: Economic growth must be pursued alongside environmental protection and social

[15] United Nations, *supra* note 1.

progress.[16] Sustainable development, therefore, requires an integrated approach to mobilize financial resources towards SDGs. In this regard, FDI has been identified as a significant source of external finance for many countries, especially developing economies, to achieve the multiple goals of eradicating poverty, effectuating economic growth, protecting the environment, and consequently promoting sustainable development.[17] Here are some keyways in which FDI is argued to contribute to sustainable development:

- Economic Growth and Job Creation: FDI can stimulate economic growth in host countries by bringing in capital, technology, and expertise. This can lead to the creation of new businesses, industries, and employment opportunities, which contribute to poverty reduction and improved living standards.[18]
- Technology Transfer and Innovation: FDI often involves the transfer of advanced technologies, know-how, and managerial practices from investor countries to host countries. This can enhance productivity, efficiency, and competitiveness, supporting sustainable industrialization and innovation in various sectors.[19]

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[16] Gordon argues that, since the concept of sustainable development recognizes poverty as major cause and effect of environmental degradation, it "purported to align the desire for development with concerns for the environment in a manner that allowed them to co-exist"; Ruth Gordon, "Unsustainable Development" in Shawkat Alam et al, eds, *International Environmental Law and the Global South* (New York: Cambridge University Press, 2015) at 61.

[17] There are also numerous empirical research publications analyzing the positive impact of FDI on SDGs. For instance, Radovan Kastratović, "Impact of foreign direct investment on greenhouse gas Emissions in Agriculture of Developing Countries" (2019) 63:3 Australian Journal of Agricultural and Resource Economics 620–642 provides empirical data indicating a positive impact of foreign direct investment in agriculture on the carbon-dioxide-equivalent emission intensity in developing countries. See also Andrew Newcombe, "Sustainable Development and Investment Treaty Law" (2007) The Journal of World Investment & Trade 357–407.

[18] The OECD, in its 2019 publication, *FDI Qualities Indicators*, noted that governments must consider FDI as part of addressing the challenges of bringing about socio-economic progress and environmental sustainability. FDIs can play a crucial role in making progress toward SDGs as it "offers a range of technological and financial resources that can raise productivity, create jobs, boost exports, spread knowledge, trigger innovation, improve living standards and, more generally, advance progress towards the 2030 Agenda": Organisation for Economic Co-Operation and Development (OECD), *FDI Qualities Indicators: Measuring the Sustainable Development Impacts of Investment* (2019) at 3. And more recently, in 2021, the OECD articulated that, because of the COVID-19 pandemic and significant drop in private investment flows, an average annual SDG funding gap has increased by 70% in 2020. It then notes "achieving the Sustainable Development Goals (SDGs) … requires an acceleration in financing these global objectives… [and] foreign direct investment (FDI) is an important source of finance for inclusive and sustainable development": Organisation for Economic Co-Operation and Development (OECD), *FDI Qualities Policy Toolkit: Policies for Improving the Sustainable Development Impacts of Investment* (2021) at 6.

[19] The United Nations Conference on Trade and Development estimates that between US$ 5 and 7 trillion worth of investment annually is needed to achieve SDGs, including those necessary for infrastructure, clean energy, water, sanitation, and agriculture: United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2014: Investing in the SDGs: An Action Plan* (2014) at iii.

- Infrastructure Development: FDI can contribute to the development of infrastructure such as transportation, energy, and telecommunications. Improved infrastructure is essential for sustainable economic growth, social development, and enhanced access to basic services.
- Sustainable Energy and Clean Technologies: FDI can drive investments in renewable energy sources, energy efficiency, and clean technologies. This promotes the transition to a low-carbon economy, reduces greenhouse gas emissions, and mitigates the impacts of climate change.[20]
- Environmental Conservation and Resource Management: Responsible and sustainable FDI can support environmental conservation efforts. Investors can adopt sustainable practices, promote resource efficiency, and contribute to biodiversity conservation and ecosystem restoration in host countries.[21]
- Social and Human Development: FDI can have positive social impacts by supporting investments in education, healthcare, and social infrastructure. This can contribute to improved access to quality education, healthcare services, and social amenities, enhancing the well-being and human development of local communities.
- Local Enterprise Development and Supply Chain Linkages: FDI can create linkages and opportunities for local businesses and suppliers to integrate into global value chains. This can promote inclusive economic growth, entrepreneurship, and capacity-building within host countries.

Accordingly, there is a body of scholarship that argues that, when aligned with sustainable development goals and practices, FDI can contribute significantly to economic growth, technological advancement, social progress, and environmental sustainability in host countries. However, it is essential to note that it is also recognized that the sustainability of FDI is far from

[20] United Nations Conference on Sustainable Development, *The Future We Want* (2012) para 127 noting "the role of foreign direct investment, international trade, and international cooperation in the transfer of environmentally sound technologies." This report recognized that mobilizing FDI is important to achieve the goals of eradicating poverty, effectuating economic growth, and promoting sustainable development.

[21] United Nations Conference on Environment and Development (UNCED), *Agenda for Environment and Development, Agenda 21* (1992), online: <https://sustainabledevelopment.un.org/content/documents/Agenda21.pdf> para 2 is calling for attention to the key role of FDI in sustainable development: "[foreign direct] investment is critical to the ability of developing countries to achieve needed economic growth … in a sustainable manner … without deteriorating … the [environmental] resource base that underpins development." The *Agenda* affirmed that investment is critical to the ability of developing countries to achieve needed economic growth to improve the welfare of their population and to meet their basic needs in a sustainable manner.

automatic or even usual. It depends, *inter alia*, on responsible investment practices, effective governance, and regulatory frameworks. Host countries need to have the right policies and institutions in place both to attract and manage FDI to maximize its positive impacts and to minimize potential adverse social and environmental effects.

1.1.2 Foreign Direct Investments

FDI is the most significant type of cross-border financial flow that gives investors a lasting interest and a compelling voice in managing their investments. FDI primarily involves transnational corporations (TNCs) that are headquartered in one country while investing in another, typically by transferring capital or other assets into the host State where the investment is established.[22] FDI can introduce capital into the host economy, increase local employment, transfer technology to the host country (directly or, more commonly, indirectly by transfer to companies, including within the same TNC structure), [23] strengthen export potential, stimulate competition in the domestic economy, [24] contribute to skills development/human capital growth,[25] and promote modernization.[26] All of these *may* contribute to higher economic growth, which some argue is the most potent tool for alleviating poverty in developing countries,[27] and improving environmental conditions in the host country.[28]

However, although "the promotion of sustainable development is ultimately the promotion of investment that improves sustainability and promotes equitable social and economic

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[22] Shyami Puvimanasinghe, "From Divided Heritage to a Common Future? International Investment Law, Human Rights, and Sustainable Development" in Shawkat Alam et al, eds, *International Environmental Law and the Global South* (New York: Cambridge University Press, 2015) at 319.
[23] Wolfgang Alschner & Elisabeth Tuerk, "The Role of International Investment Agreements in Fostering Sustainable Development" in Freya Baetens, ed, *Investment Law within International Law: Integrationist Perspectives* (Cambridge, UK: Cambridge University Press, 2013).
[24] *The Contribution of International Business Investment to the Sustainable Development Goals: Key Actors and Recent Trends*, by Michael V Gestrin (Organisation for Economic Co-Operation and Development (OECD), 2019) at 5.
[25] Puvimanasinghe, *supra* note 22.
[26] For recent trends on FDI inflows, see also United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2018* (2018), online: <https://unctad.org/system/files/official-document/wir2018_en.pdf>.
[27] Patricia McKinstry Robin, "The BIT Won't Bite: The American Bilateral Investment Treaty Program" (1983) 33 American University Law Review 931.
[28] Organization for Economic Co-Operation and Development (OECD), *Foreign Direct Investment for Development* (2002) at 5. Whether or not the generated growth is in part dependent on the net extraction of value which can be negative if the value taken out of the host economy—e.g. by transfer pricing, tax avoidance measures, reliance on government subsidies or direct infrastructure provision, and so on—is greater than the economic value left behind in the form of wages, royalties, taxes, and economic multiplier effects.

development,"[29] all countries are not on a level playing field to attract foreign investment. The benefits of FDI do not accrue automatically and evenly across countries, sectors, and local communities. On the contrary, the flow of FDI mostly depends on various complex factors, such as policies under which foreign investments are regulated and overall country conditions from an economic-risk perspective. The following section focuses on one of the steps governments commonly take in attracting foreign investments: concluding IIAs that guarantee specific standards of treatment for foreign investors and offer foreign investors the recourse to ISDS tribunals to remedy any violation of these standards by host States.

1.1.2.1 Policy Context: International Investment Agreements

As noted already, the potential contribution of FDI to sustainable development is not a given; among countries receiving FDI, some have benefited more than others.[30] Developing and least-developed countries, in particular, have pressing needs for more FDI, but foreign investors show much more reluctance to invest in developing countries than developed ones. The most common factors that can contribute to this reluctance are the higher levels of political and legal risks in developing countries compared to more stable and established economies.[31] These risks include political instability, changes in government, corruption, weak rule of law, inadequate protection of property rights, and arbitrary or inconsistent application of laws and regulations. Even more specifically, "[t]he quality of institutions, and in particular, the degree of protection of property rights, are key in determining the expected return to foreign investors. Countries with relatively poor legal protection of assets, and a high degree of political instability, generally exhibit high rates of expropriation and this makes investment less attractive."[32] These factors can increase investment risks and reduce the attractiveness of the investment environment for foreign investors to commit their capital to the economy of developing countries. Accordingly, investors make choices regarding the placement of their resources mostly based on one key element of the notion of security of investment:

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[29] *Investment Treaties & Why They Matter to Sustainable Development: Questions & Answers*, by Nathalie Bernasco Ni-osterwalder et al (International Institute for Sustainable Development (IISD), 2012) at 1.
[30] Nafisat Olabisi & Yingqi Wei, "Designing Effective Policy to Achieve Sustainable Development Impact of FDI: The Case of Sub-Saharan Africa" (2025) 8:1 Journal of International Business Policy 33–52.
[31] Global Investment Competitiveness Report 2017/2018: Foreign Investor Perspectives and Policy Implications, by The World Bank (Washington, D.C.: The World Bank, 2018) at 23.
[32] Marina Azzimonti & Pierre-Daniel G Sarte, "Barriers to Foreign Direct Investment Under Political Instability" (2007) 93:3 Economic Quarterly 287–315 at 287.

> Private investors invest to make profits and not for reasons of benevolence. Thus, if they make profits they expect, albeit not unnaturally, to keep them, subject to payment of appropriate taxes to the local authorities; if they acquire property they expect to be entitled to keep it. The feeling of insecurity in these respects is, perhaps, the major deterrent to the flow of direct foreign investment in less-developed countries (LDC[s]).[33]

Since the mid-1980s, developing countries have begun to perceive TNCs no longer as part of the problem but increasingly as part of the solution for economic growth by bringing not only much-needed capital to stimulate development. More importantly, developing countries have recognized that attracting FDI significantly depends on political/legal stability, which is often enough not present in any substantial measure in their policy frameworks.[34]

Therefore, governments and policymakers seek to address these challenges by implementing reforms, improving governance, enhancing legal frameworks, and creating more investor-friendly environments to attract foreign investment. Consequently, to address foreign investors' concerns about being expropriated in host States as a consequence of those States' political/legal instability, developing countries have sought to establish transparent, broad, and adequate investment policies. Developing countries have modernized their investment codes and adopted IIAs to increase capacity-building measures that focus on assisting stronger competencies in attracting FDI.[35] On the other hand, capital-exporting States have also negotiated IIAs as a response, on a substantive plane, to the uncertainties and perceived inadequacies of national law governing host States' responsibility for injuries to aliens and property and, on a procedural plane, to the lack of faith in either State-to-State espousal of claims or local courts as dispute settlement mechanisms.[36]

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[33] Adeoye Akinsanya, "International Protection of Direct Foreign Investments in the Third World" (1987) 36:1 The International and Comparative Law Quarterly 58–75 at 58.
[34] Graham Mayeda, "Sustainable International Investment Agreements: Challenges and Solutions for Developing Countries" in Marie-Claire Cordonier Segger, Markus Gehring & Andrew Newcombe, eds, *Sustainable Development in World Investment Law* (Kluwer Law International, 2011).
[35] Markus Gehring & Avidan Kent, "International Investment Agreements and the Emerging Green Economy: Rising to the Challenge" in Freya Baetens, ed, *Investment Law within International Law Integrationist Perspectives* (Cambridge, UK: Cambridge University Press, 2013); Phillipe Kahn, "The Law Applicable to Foreign Investments: The Contribution of the World Bank Convention on the Settlement of Investment Disputes" (1968) 44:1 Indiana Law Journal.
[36] Newcombe, *supra* note 17.

IIAs play a crucial role in promoting and protecting investors from one State (home State) to invest in the territory of the other State (host State).[37] They are designed to provide legal protection and promote a favorable investment-related legal environment, particularly for foreign direct investment venturing into large infrastructure projects in developing countries.[38] IIAs have existed since the 1960s, though it was not until the 1990s that they increased dramatically in number and became a critical component of the global investment governance regime.[39] As of September 2024, over 2500 IIAs are in force,[40] mainly in the form of bilateral investment treaties (BIT),[41] as a supplementary (or even substitute) regulatory means to that of host States' national investment policies to facilitate FDI with the notion of safeguarding foreign investments.[42] Investment agreements, therefore, are expected to provide a reliable policy framework to facilitate decision-making by companies and improve their ability to secure the necessary funding from financial intermediaries to enable their investment.

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[37] Among empirical researches, the UNCTAD report provides an in-depth analysis of how different IIA such as North America Free Trade Agreement (NAFTA) and European investment agreement can increase the flow of FDI: United Nations Conference on Trade and Development (UNCTAD), *The Role of International Investment Agreements in Attracting Foreign Direct Investment to Developing Countries* (2009), online: <https://unctad.org/system/files/official-document/diaeia20095_en.pdf>. See also Jonathan Bonnitcha, Lauge N Skovgaard Poulsen & Michael Waibel, *The Political Economy of the Investment Treaty Regime* (Oxford, UK: Oxford University Press, 2017) that suggests investment treaties do have some positive impact on FDI inflows. These publications note that, among studies that do find a positive impact of investment treaties on FDI, different studies reach contradictory findings about the circumstances in which investment treaties are likely to have a positive impact on FDI.

[38] Kenneth J Vandevelde, "A Brief History of International Investment Agreements" in Karl P Sauvant & Lisa E Sachs, eds, *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows* (Oxford University Press, 2009).

[39] The number of BITs rapidly increased from 385 at the end of the 1980s to 1,857 by the end of the 1990s: Calvin A Hamilton & Paula I Rochwerger, "Trade and Investment: Foreign Direct Investment through Bilateral and Multilateral Treaties" (2005) 18 New York International Law Review.

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[41] Bilateral investment treaties (BITs), which are the most common form of IIAs, are widely negotiated between two countries in order to facilitate foreign investment by safeguarding investors in host States. According to Sacerdoti, "the stated purpose of these BITs is to promote and protect foreign (direct) investments": Giorgio Sacerdoti, "Investment Protection and Sustainable Development: Key Issues" in Steffen Hindelang & Markus Krajewski, eds, *Shifting Paradigms in International Investment Law: More Balanced, Less Isolated, Increasingly Diversified* (Oxford: Oxford University Press, 2016) at 28.

[42] United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2003: FDI Policies for Development: National and International Perspectives* (2003), online: <https://unctad.org/system/files/official-document/wir2003_en.pdf> at 171 notes that "[m]ost host countries conclude international investment agreements … mainly to help attract FDIs to further their development, … to make the regulatory framework for FDIs in host countries more transparent, stable, predictable and secure … and to reduce obstacles to future FDIs flows."

To reduce political risks and surge host States' attractiveness, IIAs typically grant foreign investors substantive protections and provide treatment standards that host States must respect.[43] By granting foreign investors access to ISDS tribunals in the event of investment agreement violations, host States go beyond merely accepting legal obligations—they also demonstrate a firm commitment to enforcement. This access to legal recourse strengthens the credibility of IIAs and, in turn, enhances foreign investors' confidence to invest in host States.[44] Therefore, IIAs include "a number of important components to the policy and institutional determinants for FDI, and thereby contribute to enhancing the attractiveness of countries. In particular, they improve investment protection and add to the security, transparency, stability, and predictability of the investment framework,"[45] by the means of:

1. several pro-investment provisions introducing treatment standards for the protection of foreign investments in host States; and
2. an investor-State dispute settlement tribunal (ISDS) that enables foreign investors to bring claims against host States for alleged violations of one or more investment protection standards.

1.1.2.1.1 Investment-Protection Standards

IIAs impose considerable obligations of good governance on host States and set forth the specific promises that host States owe to protected foreign investors. These obligations are articulated through several provisions that introduce investment protection standards to promote FDI and shield foreign investors from illegal regulatory measures that are taken by host States.[46] These substantive treatment standards commonly include, but are not limited to:

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[43] According to the IISD report, empirical evidence does not show that IIAs actually stimulate new investments, let alone demonstrate that those investments benefit host countries: *Assessing the Impacts of Investment Treaties: Overview of the Evidence*, by Jonathan Bonnitcha (International Institute for Sustainable Development (IISD), 2017). A 2020 meta-analysis of 74 empirical studies also found that the effect of IIA on FDI is very small: Josef C Brada, Zdenek Drabek & Ichiro Iwasaki, "Does investor protection increase Foreign Direct Investment? A Meta-Analysis" (2021) 35:1 Journal of Economic Surveys 34–70. While there is no clear evidence that IIA stimulates new investment flows, it may affect how beneficially (or not) investments are structured. Against recurrent concerns that IIA is not effective enough in promoting inflows of FDI, the objective of this study is to reassess the impact of IIA on SDGs in a qualitative sense whatever the quantitative picture may be. Since IIA is a key instrument in the strategies of most countries, in particular developing countries, to attract foreign investment, policymakers and scholars need to know what role these agreements play in relation to forwarding sustainable development.

[44] Kahn, "The Law Applicable to Foreign Investments", *supra* note 35.

[45] United Nations Conference on Trade and Development (UNCTAD), *supra* note 37 at xii.

[46] Ronald Klager, ""Fair and Equitable Treatment" and Sustainable Development" in *Sustainable Development in World Investment Law* (Kluwer Law International, 2011) at 238.

- Non-discrimination.
- Fair and equitable treatment.
- Lawful expropriation.

The "non-discrimination" requirement with respect to the treatment of protected investors and investments is the most common investment protection standard that IIAs generally contain. There are two obligations associated with the requirement of non-discrimination: "national treatment" and "most-favored-nation treatment."[47] The obligation of national treatment requires the host State to give protected investments and investors treatment that is no less favorable than the treatment that it accords to national investors/investments in like circumstances. The obligation of most-favored-nation treatment also requires the host State to give protected investments and investors treatment that is no less favorable than the treatment that it accords to the investments and investors of any third State in like circumstances.

Another provision is the "fair and equitable treatment" standard that is linked to the so-called "minimum standard of treatment."[48] Alongside the protection against uncompensated expropriation, the minimum standard of treatment is a customary international law on the protection of aliens and on state responsibility establishes a minimum level of treatment to be given to protected investors and their investments.[49] As opposed to the *relative* standards embodied in national treatment and most favoured nation principles which define the required treatment by reference to the treatment accorded to other investment, the fair and equitable treatment is an *absolute* standard of treatment that its exact meaning has to be determined, by reference to specific circumstances of application. The language, scope, and meaning of the fair and equitable treatment standard may vary among IIAs; thus, scholarly accounts and arbitral practices often reached different conclusions about the content of this standard and do not support

[47] Federico Ortino, "Non-Discriminatory Treatment in Investment Disputes" in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann & Francesco Francioni, eds, *Human Rights in International Investment Law and Arbitration* (Oxford University Press, 2009) 344.
[48] See Martins Paparinskis, *The International Minimum Standard and Fair and Equitable Treatment* (Oxford University Press, 2013); Josef Ostřanský, "Fair and Equitable Treatment" in David Schneiderman & Gus Van Harten, eds, *Rethinking Investment Law* (Oxford University Press, 2023) 126.
[49] Ioana Knoll-Tudor, "The Fair and Equitable Treatment Standard and Human Rights Norms" in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann & Francesco Francioni, eds, *Human Rights in International Investment Law and Arbitration* (Oxford University Press, 2009) 310.

any stable and clearly ascertainable meaning. However, the tribunal in *Waste Management, Inc. v. United Mexican States (2004)* made one of the more comprehensive efforts to contextualize legitimate expectations, legal stability, arbitrariness, and transparency as the most controversial elements of the fair and equitable treatment standard:

> Taken together, the S.D. Myers, Mondev, ADF and Loewen cases suggest that the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.[50]

Without using the term of "legitimate expectation," the last sentence encapsulates this oft-used doctrine which tribunals have understood to flow from the ideas of unfairness or injustice that precede that sentence. Accordingly, the fair and equitable treatment standard protects foreign investors in a fairly wide variety of situations—when there has been a fundamental change in the host economy's law that is contrary to the investor's legitimate expectations; transparency has been absent in the legal process or actions of the host economy; there has been harassment, coercion, abuse of power or bad faith conduct by the host economy; and/or the actions of the host economy can be labeled as arbitrary, disproportionate, or inconsistent.

Last but not least, the requirement for "lawful expropriation" is one of the main standards included in IIAs in order to protect foreign investors against the expropriatory measures of host States.[51] According to investment treaties, States can lawfully expropriate property from foreign investors in either a direct or an indirect manner. Direct expropriation, which happens when investment ownership/title is transferred from foreign investors to host States, is lawful only if States comply with specific legal requirements: "(1) done for a public purpose, (2) cannot be discriminatory, (3) should be carried out according to the due process of law, and (4) needs to be

[50] *Waste Management v. United Mexican States (II),* ICSID Case No ARB(AF)/00/3, Award 30 April 2004, para 98.
[51] The term "expropriatory," while not found in standard dictionaries, is commonly used in legal contexts. See Andrew Newcombe, *Regulatory Expropriation, Investment Protection and International Law, When Is Government Regulation Expropriatory and When Should Compensation be Paid?* (Doctoral Thesis, University of Toronto, 1999).

followed by appropriate compensation."[52] Unlawful expropriation occurs where one or more of these requirements have not been met, including inadequate compensation that can be remedied in an ISDS proceeding under with an award of greater compensation.[53]

Since an official act that takes the title of foreign investments could cause an unbearable negative reputation for host States as a venue for foreign investment, indirect expropriations have gained importance.[54] Indirect expropriation occurs without any transfer of investment ownership/title; rather, it involves state conduct that makes the economic activity legally impossible or simply uneconomic for investors.[55] In the considerably more obscure and complex circumstances of indirect expropriation, ISDS tribunals protect foreign investors against host States' regulatory measures taken with effects equivalent to or tantamount to a direct expropriation.[56] As explained by Moreno Rodríguez, "[i]ndirect expropriations always involve prior assurances given to an investor followed by government action that wholly or significantly deprives them of their reasonable expectations regarding the investment."[57] This makes the dispute settlement a hard task as ISDS tribunals need to distinguish indirect expropriation from legitimate regulation. Furthermore, since indirect expropriation case law often includes concepts such as discrimination and due process in its terms—blurring the lines between expropriation and other standards of treatment such as fair and equitable treatment standard—it is challenging for ISDS tribunals to decide which provision is violated by host States (resulting, not uncommonly, in tribunals finding a violation of more than one standard of treatment using essentially the same reasons for breach). In the following sections, I discuss this issue in detail.

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[52] Nicolás M Perrone, "Expropriation" in David Schneiderman & Gus Van Harten, eds, *Rethinking Investment Law* (Oxford University Press, 2023) 64 at 74.
[53] José Antonio Moreno Rodríguez, *Private (And Public) International Law in Investment Arbitration (Volume 429)* (Collected Courses of the Hague Academy of International Law, 2023) at 99.
[54] Rudolf Dolzer, Ursula Kriebaum & Christoph Schreuer, *Principles of International Investment Law* (United Kingdom: Oxford University Press, 2022) at 101.
[55] Rudolf Dolzer, "Indirect Expropriation of Alien Property" (1986) 1:1 ICSID Review - Foreign Investment Law Journal 41–65.
[56] Yucong Wang, "The Protection of Public Morals as an Exception to Indirect Expropriation: Opening the Floodgates to New, Eclectic Moral Crusades?" (2022) 23:1 Melbourne Journal of International Law.
[57] Moreno Rodríguez, *supra* note 53 at 138.

All these investment-protection standards can be enforced through the ISDS mechanisms included in IIAs. Along with investment-protection standards, IIAs entitle foreign investors to bring a claim before ISDS tribunals and seek remedies if they believe their rights under these standards have been violated by host States. ISDS tribunals then assess whether measures taken by host States have violated their obligations under IIAs and, if yes, oblige host States to compensate foreign investors. From the perspective of both investor and capital-exporting States as well as capital-importing States that have committed themselves to IIAs, ISDS tribunals contribute to a stable and predictable investment environment, promoting FDI and encouraging the economic growth of host States.

1.1.2.1.2 Investor-State Dispute Settlement Tribunals

Until the late 1990s, IIAs existed in a sort of policy backwater, and foreign investors seldom invoked their investment-protection standards; thus, it was difficult to establish whether IIAs were indeed doing their job of attracting more foreign investment. However, over the last two decades, among the tools used to protect foreign investors and their investments under IIAs, ISDS tribunals have been increasingly used by foreign investors to bring a claim directly against the government of host States and to enforce their rights without the support or even knowledge of their home State.[58] By having recourse to ISDS tribunals, foreign investors no longer have to rely on their home States to espouse their claims in international courts or use local courts to address their grievances.

In neither the international nor domestic arenas is there a jurisdiction indisputably competent to settle investment disputes. The International Court of Justice (ICJ) deals with the litigation between States—and with general international law matters referred to it by international organizations by way of the advisory opinion procedure—and is not open to suits by or against private parties. Thus, it cannot resolve disputes between investors and host States unless framed as a claim of one State to protect its corporate national's rights against another State's conduct—in which case, a host of other jurisdictional carve-outs by States from the reach of the ICJ's

[58] Burzū Ṣabāḥī, Noah Rubins & Don Wallace, *Investor-State Arbitration*, second edn (Oxford University Press, 2019) at 4.

Statute mean such claims have been few and far between.[59] At the national level, the domestic courts of host States, which generally would be jurisdictionally competent as a matter of law, are viewed with suspicion by investors who may doubt their impartiality. The courts of investors' home States are also viewed with the same suspicion by host States, who find that these courts may give priority to the interests of their own national investors over those of host States were a foreign State seeks to sue[60] from the perspective of the investor as an investor in its home-state courts, it runs up against the law around foreign State immunity and the scope of the commercial exception recognized by in many States' state-immunity legislation.

Thus, in an investor-state dispute where an IIA is in place, the foreign investor bypasses both diplomatic espousal by its home State and adjudication by local courts[61]—at least initially—and seeks enforcement of the investment-protection provisions included in the relevant IIAs through the binding international arbitration of ISDS tribunals.[62] I say "at least, initially" because state court systems can come back into the picture following an ISDS tribunal award by enforcing the award as if it were a foreign judgment, where that State's legislature has implemented such arbitration-enforcement private international rules in domestic law and where sovereign immunity rules allow (e.g., if they allow awards to be enforced against state-owned commercial entities' assets in a foreign State).

To find a procedure that brings a judicial solution to the particularities of investor-state disputes, capital-exporting States, in cooperation with the World Bank, have developed a set of legal norms for ISDS tribunals as (what is assumed to be) a neutral forum for binding international

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[59] *Barcelona Traction, Light and Power Company, Limited (Belgium v Spain),* International Court of Justice (ICJ), Judgment 5 February 1970.
[60] Rafiqul Islam, "History of the North-South Divide in International Law: Colonial Discourses, Sovereignty, and Self-Determination" in Shawkat Alam et al, eds, *International Environmental Law and the Global South* (New York: Cambridge University Press, 2015).
[61] ISDS tribunals address two main challenges of domestic courts: domestic court mechanisms vary among countries and foreign investors could be concerned about their effectiveness; and domestic courts may not be fully independent and may be biased against foreign investors.
[62] Investment tribunals "grant private investors the right to request the establishment of an international arbitration tribunal against a sovereign State," Andreas R Ziegler, "Towards Better BITs?–Making International Investment Law Responsive to Sustainable Development Objectives: An Introduction" (2014) 15:5 The Journal of World Investment & Trade 803 at 804.

arbitration. These norms are included in the International Center for the Settlement of Investment Disputes (ICSID) Convention, on 18 March 1965, to promote confidence between IIAs' parties.

ICSID is a specialized institution that resolves investment disputes between foreign investors and host States. The ICSID Convention provides a comprehensive framework and legal basis for establishing ISDS proceedings and offers institutional support and services to facilitate the resolution of investment disputes between investors and member States. The ICSID Convention grants ISDS tribunals exclusive jurisdiction over investment disputes between an investor from one contracting State and another. This means that if both the investor's home country and the host country are parties to the ICSID Convention, the investor can initiate ISDS proceedings under ICSID rules. The ISDS tribunals typically comprise three private parties (arbitrators): one arbitrator appointed by the investor, one by the host country, and a neutral arbitrator appointed jointly by both parties. The tribunals have the authority to determine whether a violation of an IIA has occurred, and if so, they can order compensation to be paid to the investor or other appropriate remedies.

As of January 2024, 165 countries have signed the Convention, most of which included an ICSID arbitration clause in their IIAs. Moreover, as of 30 Jun 2023 (since the Convention entered into force on 14 October 1966), there have been almost 933 claims brought by investors before ISDS tribunals.[63] ICSID situates this phenomenon as a significant step toward promoting an atmosphere of confidence and thus stimulating a more significant flow of private international capital into those countries that wish to attract it.[64] The ICSID system does not end with these 933 tribunal claims and those to come. Another feature at least as necessary is the recourse to national legal systems after the ISDS award. One step beyond the ISDS tribunals lie the local courts (whether of the investor's home State, the host State, or third States where assets may lie) that carry out the recognition and enforcement of ISDS tribunal awards along the lines of recognition and enforcement of awards in commercial disputes by national courts under the rules

[63] International Centre for Settlement of Investment Disputes (ICSID), *ICSID's Biannual Caseload Statistics: 2023-2* (2023), online: <https://icsid.worldbank.org/sites/default/files/publications/2023.ENG_The_ICSID_Caseload_Statistics_Issue.2_ENG.pdf>.
[64] International Centre for Settlement of Investment Disputes (ICSID), *ICSID Convention, Regulations and Rules* (2006), online: <https://icsid.worldbank.org/sites/default/files/ICSID_Convention_EN.pdf> para 9.

of private international law (conflict of laws)–but with even greater certainty and effectiveness. ICSID awards, which are the decisions issued by ICSID tribunals benefit from a unique treaty-enforcement mechanism under the ICSID Convention. The decisions of ICSID tribunals are automatically enforceable in the territories of contracting States, all of which are bound by their status as ICSID Convention parties to ensure that the Convention either has direct effect in their local law or implemented by national legislation. This streamlined enforcement process greatly enhances the effectiveness and enforceability of ISDS decisions.[65]

Viewed on their own terms, ICSID tribunals are meant to shield foreign investors against the discriminatory judicial system of host States and their regulatory instability expropriating the investments. In tandem with the substantive investment-protection standards, "the main purpose of ISDS mechanisms … is to protect foreign investors and thereby encourage increased investment flows between the signatory countries."[66] By settling disputes arising from of IIAs violations, ISDS tribunals have become a powerful legal tool for foreign investors to achieve policy objectives that suit their international interests. This arbitration mechanism allows foreign investors to bring claims before ISDS tribunals to recoup their losses if their investments have been economically impaired by the host States' breach of IIAs. The following case law analyses provide illustrations as to how ISDS tribunals protect foreign investors against host States for alleged violations of one or more treatment standards for investment protection. Each of the selected cases is also an example of the standard functioning of these tribunals in contexts that involve, in self-evident ways, high stakes for sustainable development.

1.1.2.1.2.1 Case Law

A case study of *Ioan Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L., and S.C. Multipack S.R.L. v. Romania (2013)* shows how the "fair and equitable treatment" standard can protect foreign investors.[67] By way of very general summary of this case, the investors reasonably expected that the law prevailing at the time the investment will remain unchanged

[65] Tamlyn Mills & Andrew Battisson, "Recognition, Enforcement and Recovery of Investment Treaty Awards: Part I" (2022) 18 International Arbitration Report.
[66] Alexandre Gauthier, *Investor-State Dispute Settlement Mechanisms: What Is Their History and Where Are They Going?* (2016) at 1.
[67] *Ioan Micula, Viorel Micula, SC European Food SA, SC Starmill SRL and SC Multipack SRL v. Romania [I],* ICSID Case No ARB/05/20, Award 11 December 2013.

over the lifetime of the investment and thus they made their investment in reliance on that law. However, later on, the host State took actions contrary to the legitimate expectation of the investors through a change in the law. This generated financial burdens on the investors. The ISDS tribunal found that, by changing the law, Romania had violated the legitimate expectations of the foreign investors who reasonably relied on incentives in place at the time of the investment remaining unchanged. It then noted that such breach of legitimate expectations violated Romania's obligation under Article 2(3) of the BIT to afford the investors fair and equitable treatment. The tribunal ruled that Romania had to compensate the foreign investor's economic losses occasioned by the breach of the standard. What follows is a more detailed discussion of the case.

Ioan Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L. v. Romania

In 1998, Romania enacted Emergency Government Ordinance 24/1998 ("EGO 24") that established the legislative framework for the granting of certain incentives to investors investing in certain "disfavored" regions.[68] In particular, it provided preferential subsidies, as well as exemptions from customs duties (e.g., the import of raw foodstuffs) and exemptions from value-added taxes and taxes on profits for investments made in disfavored regions of Romania. Romania designated the Ştei-Nucet region as a disfavored region for a period of ten years, starting on 1 April 1999, and stipulated that all incentives offered under EGO 24 would be available to investors in the Ştei-Nucet region. In reliance on these incentives and the expectation that they were supposed to be maintained for a 10-year period, Ioan Micula, Viorel Micula, S.C. European Food S.A., S.C. Starmill S.R.L., and S.C. Multipack S.R.L made substantial investments by establishing a series of food processing plants in the Ştei-Nucet-Drâgâneşti disfavored region in northwestern Romania. However, in 2000, the European Council, acting in relation to the EU's enlargement process, determined that the EGO 24 was an "incompatible aid schemes for new entrants" and required the Romanian Competition

[68] For the list of advantages granted to the investor under EGO 24, see para 148 of *Ioan Micula, Viorel Micula, SC European Food SA, SC Starmill SRL and SC Multipack SRL v. Romania [I],* ICSID Case No ARB/05/20, Award 11 December 2013.

Council to eliminate EGO 24 with immediate effect. On 12 January 2004, Prime Minister Nastase revoked the incentives regime provided by EGO 24 due to EU requirements in order to complete its accession to the EU. This revocation which became effective on 22 February 2005 imposed financial losses on the investors as a result of which they brought arbitration proceedings against Romania before the ISDS tribunal.

The investors claimed that the host State violated the "fair and equitable treatment" standard included in the investment treaty between the Government of the Kingdom of Sweden and the Government of Romania on the Promotion and Reciprocal Protection of Investments. They contend that the premature revocation of the EGO 24 incentives undermined the investors' legitimate expectations, upset the stability of the regulatory regime, lacked transparency and consistency, and was taken in bad faith, and therefore breached Romania's obligation under Article 2(3) of the BIT to afford the investors fair and equitable treatment: Each Contracting Party shall at all times ensure fair and equitable treatment of the investments by investors of the other Contracting Party and shall not impair the management, maintenance, use, enjoyment or disposal thereof, as well as the acquisition of goods and services or the sale of their production, through unreasonable or discriminatory measures. The investors contended that "[i]n the course of enacting, promoting and implementing the EGO 24 regime, the Respondent made unambiguous and binding commitments to foreign investors, the Micula brothers, that they would be granted a number of incentives for a 10 year period in return for making certain large investments in one of the poorest and least developed regions of Romania."[69] They explained that Romania's binding commitment to provide the incentives to the investors until 1 April 2009 gave rise to a right to receive those incentives until that date, or at least generated a legitimate expectation that they would benefit from those incentives until that date. However, Romania's revocation of these incentives effective 22 February 2005 (approximately 4 years before they were set to expire) breached that commitment or undermined that legitimate expectation.

In its defence, Romania contended that the BIT does not require the Contracting States to tailor their laws and regulations to the preference of foreign investors, nor does it establish

[69] *supra* note 57 para 373.

liability for every regulatory change that has a negative impact on the foreign investors' businesses. Furthermore, it noted the BIT does not call for a regulatory standstill, and there is no warrant that a legal regime will remain unaltered. Given the absence of a clear commitment from the State to stabilize a regulatory framework, Romania argued that States are usually free to change their laws and where they practice their sovereign powers to regulate in a general, non-discriminatory way to advance public welfare (including by legislative changes), such conduct is not unfair and inequitable treatment. To justify its regulatory conducts, Romania clarified that, under the Europe Agreement, the Accession Agreement, it owed an obligation to Sweden, as an EU member, to eliminate all state aid that did not conform to EU law and distorted competition in the common market. Therefore, it is not accepted that Romania complies with an obligation to afford fair and equitable treatment to Swedish investors if such obligation would require the preservation of non-conforming State aid. In other words, "the object and purpose of the [BIT], and the context in which it was concluded as an integral part of Romania's integration into the EU, indicate that the [BIT] cannot be construed to sanction as 'unfair and inequitable' the adjustment of the Facilities in accordance with the requirements of the Europe Agreement and the *acquis Communautaire*."[70] Romania further argued that, given the factual circumstances surrounding the investment, the investors could have had no reasonable expectation that the incentives (facilities) would remain in force unchanged for ten years. The modification of the incentives was wholly predictable and equitable, given the historical context of economic transition and EU accession. In light of the plain meaning of Article 2(3), Romania contended that the investors had no legitimate expectations that were undermined by the modification of the Facilities.

In 2013, the ISDS tribunal rendered an award holding that Romania had violated the investment treaty between Sweden and Romania by failing to uphold the "fair and equitable treatment" provision and to protect the investors' legitimate expectation that they would be entitled to the EGO 24 incentives. The Tribunal found that, through an interplay of the purpose behind the EGO 24 regime, the legal norms, and Romania's conduct, Romania made a representation that created a legitimate expectation that the EGO 24 incentives would be available substantially for ten years and in the same form as they were initially offered. The

[70] *Ibid* para 486.

Tribunal considered that, in determining whether the investors had a legitimate expectation, it must take account of the accepted principle that Romania is free to amend its laws and regulations absent an assurance to the contrary. However, in this case the Tribunal found that Romania's conduct had included an element of inducement that required Romania to stand by its statements and its conduct. Romania launched a program directed to attract investors to the disfavored regions. To obtain that investment, it offered certain tax benefits for a certain amount of time. In other words, Romania created the appearance of a ten-year tax holiday for investors who decided to invest in the disadvantaged area (and this appearance conformed to what Romania did in fact wish to enact). It noted that "where the investor has acquired rights, or where the State has acted in such a way so as to generate a legitimate expectation in the investor and that investor has relied on that expectation to make its investment, action by the State that reverses or destroys those legitimate expectations will be in breach of the fair and equitable treatment standard and thus give rise to compensation."[71] In the Tribunal's view, Romania thereby made a representation that gave rise to the investors' legitimate expectation that, during this tax holiday, they would receive substantially the same benefits they were offered when they committed their investments. Consequently, the tribunal decided that the investors were entitled to compensate damages of approximately 85 million euros plus compound interest quarterly.

The case of *Eiser Infrastructure Limited and Energía Solar Luxembourg S.à r.l. v. Kingdom of Spain (2017)* is another example that explains how the arbitration mechanism can protect foreign investors against the violation of the "fair and equitable treatment" standard.[72] In a nutshell, Spain had adopted a series of regulations and incentives (RD 661/2007) to attract foreign investors in the green energy sector. However, due the economic crises, Spain revoked this form of support for renewable energy and modified the legal regime operative to the foreign investors. This governmental regulatory revocation imposed financial losses on the investor who had initially made its investment in reliance on RD 661/2007. The investor brought a claim before the ISDS tribunal and claimed that it had a legitimate expectation that the investment was entitled to certain incentives under RD 661/2007. The tribunal held Spain responsible for the breach of the

[71] *Ibid* para 667.
[72] *Eiser Infrastructure Limited and Energia Solar Luxembourg Sà.r.l v. Kingdom of Spain*, ICSID Case No ARB/13/36, Award 4 May 2017.

fair and equitable treatment under the Energy Charter Treaty (ECT). It explained that the regulatory changes drastically and abruptly revised the regime on which the investment depended in a way that destroyed its value. The tribunal found that Spain's obligation to afford investors fair and equitable treatment does protect investors from a fundamental change to the regulatory regime in a manner that does not take account of the circumstances of existing investments made in reliance on the prior regime. Spain is thus responsible to compensate the investor's financial losses. What follows is a more detailed discussion of the case.

Eiser Infrastructure Limited and Energía Solar Luxembourg S.à r.l. v. Kingdom of Spain

In 2001, the European Community adopted Directive 2001/77/CE2 on the promotion of electricity produced from renewable energy sources. The Directive required the Member States to set national targets and develop policy frameworks for growing the future consumption of renewable energy. In 2007, Spain gave effect to the Directive by implementing a new regulatory regime to create incentives for directing investments toward renewable energy sources. By adopting a very favorable renewable energy support scheme though Royal Decree (RD) 661/2007, Spain established a system of premiums and feed-in tariffs to provide a reasonable rate of return for investments in renewable energy sources. This incentive scheme encouraged foreign investors such as Eiser Infrastructure Limited and Energía Solar Luxembourg S.à r.l to venture into Spain and invest in renewable energy sources. However, the incentive scheme led to numerous investments that exceeded governmental expectations and resulted in a tariff deficit that imposed a high financial burden on Spain. The situation was further aggravated through the general financial and economic crisis of 2008. Twelve years after the European directive and six years after the start of Spain's own implementing regime, in order to stabilize the costs and revenues in the electricity sector, Spain changed its renewable energy scheme by revoking the RD 661/2007 and applied Royal Decree Law (RDL) 9/2013 that limited incentives for investments in renewable energy sources by leaving the investors the option of either the market price or the fixed rate tariff. Indeed, after Eiser had invested into the renewable energy infrastructure that Spain had tempted it to invest in, Spain completely abolished the ground rules of RD 661/2007 and introduced a

wholly new regime of RDL 9/2013, which was applicable to both new and the previously commissioned plants. This new regime was based on a completely different economic foundation to that on which Eiser based its investment and which was promised by Spain at the time of investing. As a result of these changes, at the end of 2014 the Eiser's investment was worth EUR 4 million compared to an investment of EUR 125 million initially made in the establishment of the power plants.

In 2014, Eiser took the matter to arbitration on the basis that the company had been encouraged by RD 661/2007 to invest in Spain; however, it was negatively affected by the 2013 changes in Spain despite the investor' legitimate expectations that the 2007 regime would continue. The investor argued that host State breached the Article 10(1) on "fair and equitable treatment" standard included in the Energy Charter Treaty (ECT): "Each Contracting Party shall, in accordance with the provisions of this Treaty, encourage and create stable, equitable, favourable and transparent conditions for Investors of other Contracting Parties to make Investments in its Area. Such conditions shall include a commitment to accord at all times to Investments of Investors of other Contracting Parties fair and equitable treatment." Investors contended that "the obligation to fair and equitable treatment must be construed in light of the ECT's object and purpose, which is to assure stable and transparent conditions for investment."[73] Investments in the capital-intensive energy sector require stability that gives them time to plan mid to long-term and to guarantee sufficient and reasonable profitability. In this case, Eiser was initially attracted by the 661/2007 regime safeguarding the long-term return of its investment. Eiser argued that it had legitimate expectations of stability of the RD 661/2007 regime and its promised characteristics and advantages because of the State's legal framework and other official actions confirming that the plants would receive the favorable treatments by RD 661/2007.[74] However, "the drastic changes adopted by the Respondent [Spain] defeated Claimants' legitimate expectations" that can be predicated upon the State's legal framework, and changing that framework can lead to liability.[75]

[73] *Ibid* para 357.
[74] *Ibid* para 358.
[75] *Ibid* para 358.

In its defence, Spain argued that it never made any promises or other specific commitments to Eiser that would rise to the level of legitimate expectations protected by the ECT. In host State's view, investors' expectations were not legitimate and were not protected by the ECT. Investors could not reasonably expect the freezing or "unmodifiablity" of the RD 661/2007 regime.[76] The host State made no promises or commitments in this regard, and Spanish law provides no stabilization clause freezing regulatory regimes. Spain contended that, "with proper due diligence (which Claimants' lawyers did not conduct), Claimants would have known that RD 661/2007 is an implementing regulation that could be changed."[77] It then added that case law, doctrine, and more recent jurisprudence "are now less prepared to recognize commitments on the basis of legislative frameworks," instead recognizing the need for legislative evolution as circumstances change.[78]

In 2017, the tribunal found that Spain violated its obligation under the ECT to afford investors fair and equitable treatment. Considering the context along with the object and purpose of ECT, the tribunal noted that Article 10(1) on fair and equitable treatment requires an obligation to provide fundamental stability for the essential characteristics of the legal regime relied upon by investors in making long-term investments. It further clarified that, under this Article, Spain's regulatory regimes of can be evolved and "[t]he legitimate expectations of any investor [...] [have] to include the real possibility of reasonable changes and amendments in the legal framework, made by the competent authorities within the limits of the powers conferred on them by the law."[79] It means that the ECT did not bar Spain from making appropriate changes to the regulatory regime of RD 661/2007. Thus, Eiser could not reasonably expect that Spain would have to retain the RD 661/2007 regime unchanged over three or four decades.

However, the tribunal concluded that, under Article 10(1), regulatory regimes cannot be radically altered in ways that deprive investors who invested in reliance on those regimes of their investment's value. The tribunal noted that "the ECT did protect Claimants against the

[76] *Ibid* para 359.
[77] *Ibid* para 360.
[78] *Ibid* para 359.
[79] *Ibid* para 382.

total and unreasonable change that they experienced here."[80] It stated that "Article 10(1) of the ECT entitled [Eiser] to expect that Spain would not drastically and abruptly revise the regime, on which their investment depended, in a way that destroyed its value."[81] The Tribunal admitted that Spain faced a legitimate public policy problem with its tariff deficit and adopted measures to address the situation. But it required Spain to act in a way that respected the obligations it assumed under the ECT, including the obligation to accord fair and equitable treatment to investors. The tribunal determined that changes in the regulatory regime "had a devastating effect on Claimants' investments."[82] It said that, although Spain's regulators knew that concentrated solar plants would involve heavy front-end capital investments and would be highly leveraged for the investor, the revocation of the regulatory regime that had created incentives for Eiser to invest in renewable energy sources violated its legitimate expectation.[83] For this project, Eiser borrowed substantial amounts from external lenders (Eiser's internal documents show loans to the operating companies in excess of €640 million). Eiser expected that under RD 661/2007, which offered predictable subsidized prices for sale of the plants' production (including some electricity generated by gas) and guaranteed priority of access to the grid, the project would produce long-term revenues sufficient to cover operating and capital costs and to provide an acceptable stable return to the investor. Despite these expectations, the evidence showed that Spain eliminated a favorable regulatory regime previously extended to the investor to encourage its investment in renewable energy sources. It was then replaced with an unprecedented and wholly different regulatory approach, based on wholly different premises. This new system was profoundly unfair and inequitable as applied to the investors' existing investment, stripping the investors of virtually all of the value of their investment. As a result of this, the tribunal held Spain liable to compensate damages of EUR 128 million to the investors.

The dispute settlement procedure in *BayWa r.e. Renewable Energy GmbH and BayWa r.e. Asset Holding GmbH v. Spain (2021)* case law is another example that shows how the ISDS tribunal could protect foreign investor against the violation of the "fair and equitable treatment"

[80] *Ibid* para 363.
[81] *Ibid* para 387.
[82] *Ibid* para 409.
[83] *Ibid* para 371.

standard.[84] Similar to the *Eiser* case, here, the tribunal found that the regulatory measures taken by Spain was in breach of the ECT' Article 10(1), which makes provision for the obligation to fair and equitable treatment (FET) of investments of investors in the host State. Thus, Spain is held liable in this case and ordered to pay damages to German investors in compensation for the clawback of a subsidy regime and a loss in revenue under Article 10(1) of the ECT.

1.2 ISDS Tribunals' Asymmetric Structure for Sustainable Development Goals

What has been discussed up to this point is the IIAs' potential to increase the pace of FDI in developing countries, which ultimately could facilitate the *2030 Agenda for Sustainable Development*. That discussion was followed by a debate on the legal protection afforded to FDI, with no claim that such protection clearly does or does not increase the pace of FDI. However, this chapter does not seek to weigh in on, let alone resolve, the debates in the literature on the connections between protection and flow of FDI.[85] Rather, the present focus is on the equally controversial question of whether investment protection standards and, most importantly, ICSID dispute-settlement processes do or could impede host States from achieving sustainable development goals when certain kinds of FDI projects end up in investor-state disputes. Put another way and more to the point, can and should (at least some) IIAs, with all their associated provisions, be interpreted and applied not only to protect foreign investors but also to support, in some measure, host States in their efforts to stem environmental degradation, as the violation of labour rights or local communities' health or food-harvesting rights, or the endangering of overall economic stability (and thus prospects for sustainable development)?

[84] *BayWa r.e Renewable Energy GmbH and BayWa r.e Asset Holding GmbH v. Spain,* ICSID Case No ARB/15/16, Award 25 January 2021.

[85] See the recent publication of the International Institute for Sustainable Development (IISD) doubts that IIA tends to increase inflows of FDI for developing countries. "On any reading, the evidence does not suggest that investment treaties have a strong and consistent positive impact on FDI inflows across all countries and sectors. On this basis alone, the assumption that investment treaties are a necessary and inevitable component of states' efforts to attract foreign investment is not justified. One consequence of the framing that takes the ongoing existence of investment treaties as a given is that other potential solutions to the problem of investment disputes—such as the reform or termination of investment treaties or investors' use of domestic courts—are either ignored or dismissed," *Investment Dispute Prevention and Management Agencies: Toward a More Informed Policy Discussion*, by Jonathan Bonnitcha & Zoe Phillips Williams (International Institute for Sustainable Development (IISD), 2022) at 5.

These questions have pushed IIAs into the light of public scrutiny. Further, arguments that "investment agreements can leave the poorest and most vulnerable groups worse off" have focused attention on several concerns about how ISDS tribunals operate in resolving conflicts between the goal of protecting FDI and safeguarding the environment and advancing sustainable development goals.[86]

To set the context for this controversial question, I should make it clear that incorporating repetition within this chapter serves as a conscious narrative technique chosen to underscore key themes and concepts of whether and how ISDS tribunals could hinder sustainable development goals in host States, rather than an oversight or error. This deliberate repetition aims to emphasize and reinforce critical ideas, thereby enhancing the overall coherence and impact of the narrative towards understanding the major deficiencies of ISDS tribunals in making a balance between competing priorities of investment protection and environmental consideration. Therefore, I briefly remind that, historically, developed countries pushed IIAs in order to provide legally protective measures to their domestic investors who sought to invest in riskier foreign territories outside the borders of their home States. In response, "to make the regulatory framework for FDI more transparent, stable, predictable and secure … and thereby more attractive for foreign investors," developing countries incorporated investment-protective measures into their international investment strategies for drawing foreign capitals into the territories of host States.[87] The shared premise is that, IIAs, which introduce investment protection standards and offer ISDS procedures, are sound and effective in motivating foreign investors to transfer their financial capital to host States. By obliging host States to protect foreign investors to a high degree and offering foreign investors recourse to ISDS tribunals whenever host States do not treat them in accordance with treatment standards, investors can challenge a broad range of governmental measures harming the investors' rights and ISDS tribunals can hold host States responsible to compensate foreign investors because of alleged violations of IIAs.[88]

However, this framework for thinking about IIAs, which has been in place for a long time, fails to differentiate between FDI projects that hinder the achievement of sustainable development

[86] Cordonier Segger, *supra* note 7 at 8.
[87] United Nations Conference on Trade and Development (UNCTAD), *supra* note 37 at 2.
[88] Bernasco Ni-osterwalder et al, *supra* note 29.

goals and those that align with sustainable development principles.[89] The majority of IIAs do little to address the sustainable development challenges associated with FDI projects that are facilitated and protected under IIAs.[90] As argue by the International Institute for Sustainable Development (IISD)—a non-governmental, non-profit organization that founded in 1990 to promote international policies and practices that advance sustainable development—in *Without Investment, Sustainable Development is Impossible*, IIAs have generally not been conceived through a sustainable development lens and many IIAs, especially early ones, fail to address sustainable development concerns at all.[91] This point is also emphasized by the United Nations Environment Programme in the observation that "the way many IIAs are designed at present overlook the importance of environmental and social considerations."[92] Likewise, the United Nations Conference on Trade and Development has noted, in certain circumstances investment agreements can leave developing countries and most vulnerable groups disadvantaged.[93] The lack of a sustainable development perspective in IIA-making is not limited to overlooking the importance of environmental and social considerations, but it extends to a more fundamental issue that "the investment protection function of IIAs may impede, discourage, or even prohibit government measures to ensure sustainable development."[94] Cordonier Segger warns that, although the terms agreed to in IIAs may serve to reduce barriers to investment and thus

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[89] *Ibid* at 1.

[90] It should be mentioned here that more recent IIAs are supposed not only to ensure foreign investor protection from certain government actions of host States but also to "support sustainable development by guarantying [sic] a secure and predictable 'enabling' framework for foreign investment:" Marie-Claire Cordonier Segger & Andrew Newcombe, "An Integrated Agenda for Investment Law" in Marie-Claire Cordonier Segger, Markus Gehring & Andrew Newcombe, eds, *Sustainable Development in World Investment Law* (Kluwer Law International, 2011) at 103. For instance, the Canada-Republic of Moldova BIT entered into force in 2019 with the aims of "recognizing that the promotion and the protection of investments of investors of one Party in the territory of the other Party will be conducive to the stimulation of mutually beneficial business activity, to the development of economic cooperation between them and to the promotion of sustainable development," according to its Preamble: *Agreement between the Government of Canada and the Government of the Republic of Moldova for the Promotion and Protection of Investments* (2018), online: <https://edit.wti.org/document/show/cc60d80f-237f-4aad-ac69-bce10d78825b>.

[91] International Institute for Sustainable Development (IISD), *Without Investment, Sustainable Development is Impossible* (2019).

[92] Partnership for Action on Green Economy, *International Investment Agreements & Sustainable Development: Safeguarding Policy Space & Mobilizing Investment for a Green Economy* (2018), online: <https://www.greenpolicyplatform.org/sites/default/files/downloads/resource/international_investment_agreements_sustainable_development_1.pdf> at 2. See also Alschner & Tuerk, *supra* note 23.

[93] United Nations Conference on Trade and Development (UNCTAD), *Developing Countries in World Trade* (2002); United Nations Conference on Trade and Development (UNCTAD), *Policy Coherence, Development Strategies and Integration into the World Economy* (2004).

[94] Marie-Claire Cordonier Segger & Andrew Newcombe, "An Integrated Agenda for Investment Law" in Marie-Claire Cordonier Segger, Markus Gehring & Andrew Newcombe, eds, *Sustainable Development in World Investment Law* (Kluwer Law International, 2011) at 103.

encourage economic growth, "there is concern that[,] absent due care, trade and investment promotion could lead to unnecessarily destructive impacts on the environment and on social cohesion."[95] This point is extensively discussed by Zagel who argues, in the context of African countries, "International Investment Agreements (IIAs) permit foreign investors to challenge host State measures affecting their business. … [E]ven if such measures serve sustainable development purposes, they have recently triggered extensive opposition."[96] As further discussed by Newcombe, "IIAs, in their roles as investment promotion and protection agreements, do not distinguish between investment activities that are sustainable and those that are not … [Thus,] [e]ntitlement to protection under the IIA regime does not require that the investment in question benefit the host State based on any specific qualitative or quantitative criteria."[97] This problem is worsened by the basic legal inequality between foreign investors and host States according to which investors have substantive rights without substantive obligations under IIAs.[98] Rose-Ackerman criticizes the destructive impacts of investment agreements on the environment and on social cohesion in host States due to the general understanding that, in investment law, only the investor has substantive legal rights with no corollary or parallel legal obligations.[99] Viñuales reiterates the same point that IIAs were created without due consideration of the need of host States to mitigate or adapt to climate change or implement urgent measures to protect the environment.[100] This results in the perception of "international investment law having given investors a privileged position[, which]… is evidence of States favouring investment and trade over other important societal matters and concerns, including the environment."[101]

Concerns regarding the wide scope of investment protection standards and the lack of investors' obligations under IIAs have been coupled with serious criticisms of using ISDS tribunals as

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[95] Cordonier Segger, *supra* note 7 at 9.
[96] Gudrun Monika Zagel, "International Investment Agreements (IIAs) and Sustainable Development: Are the African Reform Approaches a Possible Way out of the Global IIA Crisis?" (2020) 17:1 Manchester Journal of International Economic Law 26–47 at 27.
[97] Andrew Newcombe, "Sustainable Development and Investment Treaty Law" (2007) The Journal of World Investment & Trade 357–407 at 375.
[98] Félix Antolín Martínez, "Re-thinking the Requirement of Making an Investment in Accordance with Domestic Laws as a Substantive Right and a Cause of Action for Host States under the BITs" (2018) 22 Iuris Dictio 101–114.
[99] Susan Rose-Ackerman, "Do BITs Benefit Developing Countries?" in Catherine A Rogers & Roger P Alford, eds, *The Future of Investment Arbitration* (Oxford: Oxford University Press, 2009) 131.
[100] Jorge E Viñuales, "Foreign Investment and the Environment in International Law: Current Trends" in Kate Miles, ed, *Research Handbook on Environment and Investment Law* (Edward Elgar Publishing, 2019) 12.
[101] Gleason, *supra* note 2 at 428.

weapons to undermine sustainable development goals in host States. This criticism, central to this dissertation, raises concerns that "foreign investors often use the threat of such arbitrations to compel governments to alter or abandon regulations which may negatively impact an investor" and sustainable development in host States can be impeded in direct relation to private benefits that result from such threats.[102] Given this contextual background, I will introduce a hypothetical scenario that will serve as the focal point for the remainder of this chapter and a reference point in the subsequent chapters.

At its most general, ISDS tribunals have to resolve sustainable-development-related disputes between foreign investors, with allegations of host State violations of IIAs, and with host States defending their regulatory environmental measures. In this scenario, a host State, Country X, heavily relies on FDI in its mining sector. A transnational corporation, Company Y, invests significant capital and resources to establish a large-scale mining operation in a remote area of Country X. However, over time, it becomes evident that the mining activities of Company Y is causing severe environmental problems, including water pollution, deforestation, and habitat destruction. Local communities and environmental bodies point out concerns about the negative impacts on ecosystems, biodiversity, and the health of surrounding communities. In response to the environmental problems caused by Company Y's mining operations, the government of Country X adopts regulatory environmental measures to manage the environmental impacts of resource-intensive FDI projects by stopping the FDI activity. As a result of these regulatory environmental measures, Country X orders Company Y's mine to cease operations alongside ordering both remediation of the environment and compensation for related harm to the health and food-harvesting rights of neighboring communities as a condition for Company Y's mine to resume operations; Country X does not offer any compensation, making clear that it does not consider its action to be expropriatory but, rather, regulatory.

Deprived of enjoyment of its investment, Company Y brings a claim under an IIA that initiates a proceeding before an ISDS tribunal. Company Y accuses Country X of both of indirect expropriation of FDI and of a violation of the "fair and equitable treatment" standard included in

[102] Nathalie Bernasco Ni-osterwalder et al, Investment Treaties & Why They Matter to Sustainable Development: Questions & Answers (International Institute for Sustainable Development (IISD), 2012) at 7.

the IIA, and on one or either basis thus claims compensation for the resultant economic damages. In its defence, the government of Country X justifies its regulatory measures by referring to its public purpose of environmental protection, stating that the environmentally risky operations of Company Y that both have already harmed the environment and human rights and pose ongoing and future significant threats to the Country's natural resources, ecosystems, and the well-being of its citizens. In such a starkly framed case like this, we can easily observe how the future of environmental conditions in host States is in the hands of ISDS tribunal members who are called on by the law of IIAs to draw the line between non-compensable, environmentally-protective and lawful regulatory measures and indirect expropriation and/or unfair and inequitable treatment that is unlawful and thus requires compensation.

The clearcut nature of the facts in this scenario sharpen our ability to see what is at stake, but in their full complexity, in real-life cases like this, the outcomes are dependent on understanding:

- whether (or not) ISDS tribunals welcome environmental concerns of the host State as *procedurally admissible* and *doctrinally relevant* in their decision-making; and
- if admissible and relevant, the extent to which ISDS tribunals' embrace of environmental normativity is *substantively consequential* in terms of favourable outcomes for States versus being constrained by the combination of tribunals' readings of IIA text and tribunals' understanding of the underlying purpose of investment protection through IIA in general and a given IIA in particular.

In the following three sections, I make my contribution to scholarly arguments that revolve around the contestation that, although IIAs could be deemed an essential avenue for achieving sustainable development (through sustainability-oriented investment and sustainability-consistent operations), ISDS tribunals, on the other side of the coin, play an impeding role by pressuring host States to abandon environmental measures that they are legally entitled to adopt.[103] First, I explain the scope of my research that brackets the social, economic, and other aspects of sustainable development in order to focus more particularly on environmental-protection issues

[103] I use the term "impeding" deliberately to highlight that the effect often described in the literature as a "chilling effect" is not merely a general sense of caution over policy and law. Rather, it represents a pervasive and tangible influence that actively impedes or restricts States from taking legal risks. If this distinction appears overly subtle or seems to stretch the conventional meaning of "chilling effect," the reader may safely interpret "impeding" as synonymous with "chilling" without altering the overall argument.

within the investment sector. Second, I survey the literature on the three major general criticisms of ISDS tribunals that span all forms and consequences of investment but are also relevant to what is, generally speaking, their environmental unfriendliness. Third, and most importantly, in light of these general criticisms, I discuss how the current practices of ISDS tribunals would generally approach the issues arising from the hypothetical scenario mentioned above. ISDS tribunals have generally approached these issues in one or more of three ways: the sole effect doctrine, the regulatory power doctrine, and the investment reprisal approach. Within this third section, I scrutinize the frequent adoption of the sole effects doctrine, the restricted utilization of the regulatory power doctrine, and the infrequent recourse to the investment reprisal approach in order to assess how these tendencies hinder or diminish the environmental dimension of sustainable development in disputes concerning environmental investments.

1.2.1 The Scope of the Research

As mentioned, ISDS cases with environmental components typically involve disputes between foreign investors and host countries concerning environmental regulations, policies, or actions that may impact the investor's rights or FDI.[104] These disputes can arise in various sectors and can involve a range of issues. Here are some examples of environment-related ISDS disputes:

- Regulatory Changes: Disputes can occur when a host State implements new environmental regulations or changes existing ones that affect the operations or profitability of foreign investors. Investors may argue that these regulatory changes amount to expropriation of their assets or breach their legitimate expectations (and thus standards of fair and equitable treatment), leading to claims for compensation.
- Environmental Permits: Disputes may arise when a host State deprives foreign investors of permits related to environmental assessments, pollution control, resource extraction, or land

[104] Viñuales defines investment disputes with environmental components as disputes that arise "from the operations of investors (i) in environmental markets (e.g., land-filling, waste treatment, garbage collection, pesticides/chemicals, energy efficiency, emissions- reduction, biodiversity compensation, etc.) and/or (ii) in other activities, where their impact on the environment or on certain minorities is part of the dispute (e.g., tourism, extractive industries, pesticides/chemicals, water extraction or distribution) and/or (iii) to disputes where the application of domestic or international environmental law is at stake"; Jorge E Viñuales, "Foreign Investment and the Environment in International Law: The Current State of Play" (2016) 1 Cambridge Centre for Environment, Energy and Natural Resource Governance (C-EENRG) at 17.

use. Investors may challenge such decisions and allege that they are arbitrary, discriminatory, or not in compliance with the obligations under IIAs.

- Renewable Energy and Climate Change Policies: Disputes can arise concerning renewable energy projects, feed-in tariffs, subsidies, or incentives provided by host countries to promote clean energy. Investors may claim that changes to these policies or the withdrawal of incentives harm their investments, leading to investor-state disputes for compensation.

To clarify why my research focuses specifically on the environmental dimension of sustainable development, it is important to note at the outset that I fully acknowledge: a) the importance of all 17 SDGs in advancing the broader sustainable development agenda and all aspects of sustainable development are interdependent and mutually reinforcing; and b) the findings and analytical framework of my study can also be extended or adapted to address other aspects of sustainable development. When it comes to human rights issue, the SDGs area perhaps most closely interconnected with environmental rights, I would say that human rights, apart from being a body of norms/law that is wrapped into sustainable development, is also a broad concept that encompasses or is instrumentally related to environmental rights—such that even a limitation to the environmental aspects of sustainable development has some fairly direct overlap with the human rights aspects of sustainable development. This understanding reflects the growing recognition that a safe, clean, and healthy environment is interdependent with the enjoyment of fundamental human rights. Thus, based on these perspectives on how human rights relate to sustainable development and the environment, the arguments I make for holding investors environmentally accountable in ISDS tribunals can also support claims related to human rights violations more broadly. In other words, the same (or, at least, closely similar) legal reasoning and normative frameworks I apply to environmental harms can be used by host States when they seek to challenge an investor's human rights liability in ISDS tribunals. Given these explanations, in light of the following theoretical considerations and practical relevance, I have narrowed down the scope of my research to focus on analyzing how environmental-related disputes are resolved in ISDS tribunals:

1. Depth and specialization: By focusing on the environmental aspect of sustainable development, I can delve deeper into the topic and enhance my comprehensive understanding of this area. This allows me to conduct a more nuanced analysis with the potential to make significant contributions to knowledge in this specific domain. In this

regard, my specialized research experiences—notably, my environmental studies background—provide me with an enriched knowledge of how the environment could be adversely affected through the life cycle of foreign investment activities, of why transnational corporations undermine environmental values in their foreign investments, and in what way existing policies might promote environmentally sound investment projects.

2. Necessity and research gap: The adverse impacts of climate change have motivated States to develop environmental policies against environmentally risky activities worldwide. Based on the findings of recent reports, we can expect an increase in the use of ISDS by investors who are investing in the fuel sector and affected by governmental actions taken in accordance with such environmental policies. The *World Economic Forum's Global Risks Report 2019* explains that environmental risks such as extreme weather events[105] and climate change policy failures are perceived as the gravest global threats in the next decade.[106] Thus, environmental risk management, such as climate change management, is at the forefront of global efforts to sustain the planet.[107] In addition, in the last two decades, the number of investment disputes that have seen investors targeting environmental or climate measures has risen steeply and is expected to increase further.[108] This type of information convinces me to focus on particular ISDS cases dealing with the environmental aspect of sustainable development.
3. Relevance and practical applications: A focused study can have direct implications for practical applications or policymaking. Environmentally relevant disputes in ISDS tribunals are likely to grow in the coming years and decades. The *Net Zero by 2050: A Roadmap for the Global Energy Sector* report notes that new national/international policies are required to achieve the Paris Agreement temperature goal. [109] Climate mitigation

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[105] The annual average losses from tsunamis, tropical cyclones, flooding and wildfires related to rising global temperatures amount to hundreds of billions of dollars, Jorge E Viñuales, "Foreign Investment and the Environment in International Law: The Current State of Play" (2016) 1 Cambridge Centre for Environment, Energy and Natural Resource Governance (C-EENRG) at 17.
[106] World Economic Forum (WEF), *The Global Risks Report 2019* (2019).
[107] Organisation for Economic Co-Operation and Development (OECD), *supra* note 18 at 139.
[108] Kate Miles, "International Investment Law and the Environment: Introduction" in Kate Miles, ed, *Research Handbook on Environment and Investment Law* (Edward Elgar Publishing, 2019) 1.
[109] International Energy Agency, *Net Zero by 2050: A Roadmap for the Global Energy Sector* (2021), online: <https://www.iea.org/reports/net-zero-by-2050>.

strategies, if adopted, will lead to further "asset stranding" in both developed and developing countries. And the more compelling the need to adopt ambitious measures to protect the environment, the higher the risk of ISDS cases being brought against host States.[110] Therefore, by concentrating on the environmental aspect of sustainability, I can generate findings and recommendations that are more directly applicable to real-world scenarios and address specific challenges or opportunities within that domain.

4. Resource constraints: Research endeavors are often bound by limitations such as time, funding, and available resources. Conducting a comprehensive study of all aspects of sustainable development may be impractical and time-consuming. My Ph.D. study's limited timeframe and the dissertation's page requirements force me to emphasize only the environmental aspect of sustainable development, which makes my ultimate theoretical and practical findings distinctively applicable to foreign investors' environmental responsibility before ISDS tribunals.[111]
5. Collaboration and complementary research: Focusing on the environmental aspect of sustainable development allows me to collaborate with other researchers who specialize in the social and economic aspects of sustainable development. By collaborating with researchers in economy and social sciences, we can collectively address different facets of sustainable development, fostering interdisciplinary cooperation, and generating a more comprehensive understanding when the findings from various studies are synthesized. Thus, the findings of my research could be extensively used by researchers studying the social dimension or economic aspect of sustainable development and examining the

[110] In this context, the recent International Court of Justice Advisory Opinion (July 2025) on climate change is set to trigger a surge in investment disputes by recognizing a robust set of binding legal obligations for States, *Obligations of States in Respect of Climate Change*, International Court of Justice (ICJ), Advisory Opinion 23 July 2025. This Advisory Opinion affirms that States have legally binding obligations under both climate treaties and broader international law to take robust action against climate change, including the duty to prevent significant environmental harm and cooperate in good faith. Accordingly, States are obliged to enact environmental regulations, such as phasing out fossil fuels, which will directly harm the value of foreign investments in carbon-intensive industries. Consequently, affected investors are expected to challenge these necessary climate actions as treaty breaches, claiming indirect expropriation or unfair treatment, thereby launching a new wave of high-stakes investor-state arbitration. See the Concluding Pathways where I discuss the relevance of my dissertation to this recent landmark Advisory Opinion.

[111] While the domain of my research analysis is restricted to the environmental aspect of sustainable development, its outcomes are capable of being expanded to examine how ISDS tribunals treat the economic and social dimensions of sustainable development in their decision making or how other aspects of sustainable development could be protected by the means of ISDS tribunals. This is especially the case when, as my hypothetical shows, the environmental, the social and the economic can be closely intertwined in both the impacts of corporate conduct and state measures taken in response to impacts.

settlement of investor-state disputes concerning social and economic measures taken by host States.

1.2.2 General Criticisms of ISDS Tribunals

ISDS tribunals are meant to ensure an independent and neutral forum for resolving investor-state disputes and to provide foreign investors with a mechanism to seek legal recourse if they believe their investments have been expropriated by host States. However, to whatever extent ISDS tribunals can enhance foreign investors' confidence and prevent arbitrary actions by governments, the regulatory framework of the tribunals is widely criticized by some, if not many, host States as well as academic and activist observers as a controversial part of the global investment governance regime. In this section, I delve into the three most widespread forms of host States' discontent with (and scholarly criticism of) ISDS tribunals:

1. The exclusive access of foreign investors to ISDS as exacerbated by anti-state and anti–South biases in ISDS tribunals' decisions due to the inequitable nature of IIAs' basic structure, substantive provisions, and procedural mechanisms.
2. The breadth of investment-protection provisions included in IIAs and their chilling effects on host States' regulatory sovereignty.
3. The extensive impact of ISDS tribunals on the public budgets of host States by way of their ability to hold them liable for paying uncapped, or otherwise very high, amounts of compensation.

1.2.2.1 One-Sidedness Fused with Bias

The first criticism of the ISDS framework stems from the one-sided ability of investors to sue the government of host States. Substantive investment protection standards included in IIA "enable foreign investors to initiate arbitrations against the host States in order to settle disputes about the scope and compliance with these substantive standards."[112] According to the ICSID Convention, any covered foreign investor can bring a claim against host States and allege that their governmental decisions violated investment-protection standards included in IIAs. This process

[112] Stephan W Schill, "Private Enforcement of International Investment Law: Why We Need Investor Standing in BIT Dispute Settlement" in Michael Waibel et al, eds, *The Backlash Against Investment Arbitration Perceptions and Reality* (The Netherlands: Kluwer Law International, 2010) at 29.

exposes host States to claims from a seemingly unlimited number of individuals and entities involved in FDI projects. Potential claims are all the more unlimited due to the ways in which organization of corporate personality by choosing states of incorporation and linking companies in complex chains can mean an unpredictable entity could turn up as a *foreign* investor with access to a particular IIA treaty—and even more so here IIAs or caselaw allow multiple individual shareholders to make claims.

Since the main aim of such treaties is, indeed, to protect the investor's rights, the asymmetric nature of investment treaties prevents a host State from invoking any treaty right against an investor. Almost invariably, investment treaties themselves do not impose obligations upon investors and, accordingly, host States cannot rely on the violation of the provision of any such treaty by the investor (or even its home state) as basis to sue an investor using ISDS procedures. Although an investment treaty like the "Spain-Argentina BIT does not lay down *ratione personae* restrictions on who may bring a claim"[113] and thus "does not indicate that a State Party could not sue an investor in relation to a dispute concerning an investment,"[114] in practice, only claims based on a violation of the BIT's own provisions have been understood as admissible in ISDS tribunals. This is both because the treaty regime is understood as the full basis for the legal relationships that an ISDS process pursuant to that treaty can consider and because a state suing an investor on the basis of rules external to the treaty is an unreal possibility in the investment law world because of the assumptions general international law does not impose obligations on corporate investors. The commonly assumed bottom-line is thus that are no norms on which host States may sue foreign investors, because investment treaties do not impose obligations upon the investor and because it is taken as given that neither does general international law.[115] It will be

[113] *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, *supra* note 3 para 1145. Article X(1) of Spain-Argentina BIT provides: "Disputes arising between a Party and an investor of the other Party in connection with investments within the meaning of this Agreement shall, as far as possible, be settled amicably between the parties to the dispute," *Agreement for the Promotion and Reciprocal Protection of Investments Between the Republic of Argentina and the Kingdom of Spain* (1991), online: <https://edit.wti.org/document/show/906eff11-67f0-4fed-afb9-3f6a725b5c76>.
[114] *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, *supra* note 3 para 1143.
[115] I note here that the above criticisms of one-sidedness should not lead to the belief that a State can bring no claim under an IIA. While they cannot initiate a claim under most IIAs (but not all), in international jurisprudence, even when the right of filing counterclaims is not expressly provided for or regulated, international arbitral tribunals "have the inherent power to hear counterclaims," thus giving each party a full opportunity to be heard, *The 'Erica Lexie' Incident (Italy v India),* Permanent Court of Arbitration (PCA), Case No 2015-28, Award 21 May 2002, para 254. It

the thrust and burden of this dissertation to argue that this "given" is mistaken and that general international law can impose obligation on investors and, in some areas and on some issues, it already does.

Van Harten criticizes the openness of ISDS tribunals to investors but not to host States whose interests are affected by foreign investment, provoking discontent with the impartiality of ISDS tribunals.[116] He further argues that this one-sided access of investors to ISDS tribunals could even worsen the situation to the extent that arbitrators might be motivated to interpret the law in favor of investors in order to maintain the growth of the arbitral industry.[117] Schill and Bernasconi-Osterwalder likewise challenge the orientation of ISDS tribunals in light of the non-reciprocity of the power to sue under IIAs.[118]

Anghie goes further to note that the inequality among investors and States is not limited to claim initiation but is inherent in treaty-based negotiation that produces the IIAs in the first place.[119] In terms of inequitable negotiation, Islam ties IIAs back into a historical account of the influence of the colonial rules in shaping international law that is still evident in contemporary international law-making treaties representing the interests of the Northern States while ignoring the needs of the global South.[120] Concerning the international investment regime, he notes that the inequality of IIAs' parties "in negotiated bargaining and trade-off powers of inducement and coercions

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is the use of counterclaims that will be one of the avenues explored in this dissertation in terms of extant ways in which doctrinal evolution in States' favour can evolve. Furthermore, the *Urbaser* case law illustrates situations thereby the host State could be able to initiate a claim before ISDS tribunal and sue the investor based not on an obligation owed to it by the investor under the treaty but on the violation of international obligations imposed on foreign investors by international rules external to the treaty. In this case, the tribunal stated that "Article X of the BIT provides for a possibility of a host State submitting a claim or a counterclaim to international arbitration" without limiting the basis of that claim to the treaty alone, *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic,* ICSID Case ARB/07/26, Award 8 December 2016, *supra* note 104 para 1153.

[116] Gus Van Harten, "Investment Rules and the Denial of Change" (2010) 60:3 University of Toronto Law Journal 893.

[117] Gus Van Harten, "Perceived Bias in Investment Treaty" in Michael Waibel et al, eds, *The Backlash Against Investment Arbitration: Perceptions and Reality* (The Netherlands: Kluwer Law International, 2010).

[118] Stephan W Schill, "Do Investment Treaties Chill Unilateral State Regulation to Mitigate Climate Change?" (2007) 24:5 Journal of International Arbitration 469. Nathalie Bernasconi-Osterwalder, "Who Wins and Who Loses in Investment Arbitration? Are Investors and Host States on a Level Playing Field? The lauder/Czech Republic legacy" (2005) 6:1 The Journal of World Investment & Trade: Law, Economics, Politics 69.

[119] Antony Anghie, "Inequality, Human Rights, and the New International Economic Order" (2019) 10:3 Humanity: An International Journal of Human Rights, Humanitarianism, and Development 429.

[120] Islam, *supra* note 60.

lead[s] to the exoneration [of investors] from liability and the rigid FDI protection regime."[121] This point is also highlighted by the United Nations Economic Commission for Africa (UNECA), which points out that the root of the IIAs can be traced back to the end of colonialism: a process that was initiated by colonizer countries to protect their interests in their former colonies[122] and embraced by newly independent States "to attract greater investment and to deepen regional integration."[123] Through the IIA negotiation process, developing countries might, in various degrees of desperation, sacrifice their concerns about the downside of signing up to such gateways to corporate power in order to attract foreign investments, even as developed countries like the US take advantage of their strong bargaining position to secure treaty protection for their investors.

Sornarajah argues that the legal norms of the international investment regime embedded in colonialism have been manipulated to protect the commercial interests of capital-exporting countries in the advancement of exploiting host countries.[124] After a colonial period, "the need for a system of protection of foreign investment came to be felt by the erstwhile imperial powers which now become the exporters of capital to the former colonies and elsewhere."[125] In consequence, host countries that might suffer from irreversible harms caused by foreign investors are unable to rely on this regime to safeguard national values and as a source of financial compensation for such corporate harms.

This inequality continues to be reinforced at a higher level in ISDS tribunals, the proceedings of which take place against the backdrop of an unequal North-South divide. For instance, Chung argues that developing countries are also disadvantaged in ISDS arbitrations and investment tribunals mostly award in favor of industrialized nations.[126] Van Harten furthers such empirical studies and outlines noteworthy findings that investor arbitrators often support foreign investors,

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[121] *Ibid* at 48.
[122] See generally Muthucumaraswamy Sornarajah, *The International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2017).
[123] United Nations Economic Commission for Africa (UNECA), *Investment Policies and Bilateral Investment Treaties in Africa Investment: Implications for Regional Integration* (2016), online: <https://archive.uneca.org/sites/default/files/PublicationFiles/eng_investment_landscaping_study.pdf> at 2.
[124] Sornarajah, *supra* note 122.
[125] *Ibid* at 21.
[126] Olivia Chung, "The Lopsided International Investment Law Regime and Its Effect on the Future of Investor-State Arbitration" (2007) 47 Virginia Journal of International Law 953.

particularly those from major Western capital-exporting States, over the Third World host States.[127] His study of 140 ISDS cases shows a tendency toward resolving investment claims in favor of investors and requiring host States to compensate foreign investors for lost profits. He also reports that "in 1001 issue resolutions over 123 cases, there was evidence of a strong inclination in favor of an accentuated expansive approach if the investor was a national of a major Western capital-exporting State."[128] The preference of ISDS tribunals to uphold foreign investors and the very pro-investment structure and content of IIAs negotiated between investment-exporting States and investment-importing States then results in the regulatory chill that is the subject of the second line of criticism.

1.2.2.2 Chilling Effects on Regulatory Sovereignty

Regarding the second line of criticism, developing States, in expectation of an increasing FDI flow, limit their sovereignty in order to offer a higher level of protection to foreign investors through the adjudication procedure of ISDS tribunals.[129] In ISDS tribunals, investors have challenged a broad range of government measures as allegedly violating the investment protection provisions included in IIAs and harming the investors' rights. These measures might aim at collecting taxes, changing domestic fiscal policy, renegotiating investment contracts, banning harmful chemicals, requiring environmental impact assessments, regulating hazardous waste, governing health insurance, or improving the economic situation of minority populations.[130] In these cases, if governments are held liable for the impacts of their regulations on investors, they will either not regulate to the extent that they should or will modify or remove regulations when threatened with investor claims.

Van Harten observes that, even before questions of biased orientation arise, ISDS tribunals settle investment claims based on the standards in IIAs that are on their own terms pro-investment. As discussed earlier, these provisions then confine host States' sovereignty by prohibiting

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[127] Gus Van Harten, "Arbitrator Behaviour in Asymmetrical Adjudication (Part Two): An Examination of Hypotheses of Bias in Investment Treaty Arbitration" (2016) 53:2 Osgoode Hall Law Journal 540–586.
[128] *Ibid* at 560.
[129] Fola Adeleke, *International Investment Law and Policy in Africa: Exploring a Human Rights Based Approach to Investment Regulation and Dispute Settlement* (New York: Routledge, 2018); Barnali Choudhury, "Spinning Straw into Gold: Incorporating the Business and Human Rights Agenda into International Investment Agreements" (2017) 38:2 University of Pennsylvania Journal of International Law 425.
[130] Bernasco Ni-osterwalder et al, *supra* note 29 at 7.

"expropriation" of foreign investments, by prescribing "fair and equitable treatment" for investors, and by providing "no less favorable" treatment to the foreign business that offered to its domestic counterparts.[131] Peterson also notes that the breadth of pro-investment provisions turns ISDS tribunals into "an open invitation to unhappy investors, tempted to complain that a financial and business failure was due to improper regulation, misguided macroeconomic policy or discriminatory treatment by the host government."[132] Alschner and Tuerk reiterate that foreign investors might use pro-investment provisions enshrined in IIAs to bring a claim against measures taken by host States aimed at achieving legitimate public policies.[133] This is not simply a concern about the lawful use of IIAs' pro-investor provisions but about the use of such provisions for tenuous or bad claims simply as a means of pressure on States to change their policies or settle generously in favor of foreign investors. The abusive use of claims as a form of coercion—no different from what corporations do all the time, assisted by willing lawyers, in domestic legal systems—contributes to the chilling effects on State regulatory power.

This means that ISDS tribunals have the authority to rule on cases where foreign investors challenge a host State's regulatory environmental measures if those measures negatively impact the investor's profits. Even if the regulation is intended to protect the public interest (e.g. reducing air/water pollution), if it directly or indirectly reduces the profits of the investment, the investor may argue that it violates their protective rights under an investment treaty, and the tribunal may consider the claim. This threat of ISDS is now seen by many to have an informal chilling effect on States adopting public welfare regulations that either appear to be inconsistent with IIAs or are in a wide zone of risk for being creatively (or cynically) characterized by investors as inconsistent. Sacerdoti joins in this discussion by confirming the possibility of "the interference of legal commitments stemming out of IIAs, especially directly in favor of foreign investors, with the right and ability of host States to pursue [public] policies."[134] State sovereignty or "regulatory power"[135] presumptively allows the State to protect essential public

[131] Van Harten, *supra* note 117.
[132] William Rogers, Emergence of the International Center for Settlement of Investment Disputes (ICSID) as the Most Significant Forum for Submission of Bilateral Investment Treaty Disputes Presentation to Inter-American Development Bank Conference (2000).
[133] Alschner & Tuerk, *supra* note 23.
[134] Sacerdoti, *supra* note 41 at 27.
[135] Regulatory power includes direct statutory regulation and also is defined in each jurisdiction by the legislative body, which determines the public purposes that need to be served by legislation and that invests power in

interests from certain types of harm.[136] However, that presumption is nullified if the host State has considered that, once giving a commitment to investor protection under an IIA in the interest of its economy (and possibly of some wider sustainable development policies), it might face the hurdle of infringing the IIA when adopting a new public policy inconsistent with its initial commitment. Such tension between investment protection and the exercise of "regulatory power" indulges foreign investors with compensation (or the threat to seek it) while chilling the regulatory capacity of host States. Toby Landau, a well-known arbitration lawyer in the ISDS field, stated on an Australian radio program in 2014 that regulatory chill that deters governments from regulating in the public interest to avoid being sued by foreign investors is already happening in countries around the world:

> Without doubt, "regulatory chill", in my view, definitely exists, and there's palpable evidence of it. There are those who deny it, but I can say that in my role as counsel, on a number of occasions now I've actually been instructed by governments to advise on possible adverse implications or consequences of a particular policy in terms of investor-state (ISDS) cases.[137]

Schneiderman also asserts that there is an apparent deterrence of domestic regulation in the face of investor claims, and the investment governance regime "has as its object the placing of legal limits on the authority of government, isolating economic from political power, and assigning to investment interests the highest possible protection."[138] Schneiderman demonstrates how IIAs/BITs and ISDS essentially "constitutionalize" economic globalization whether or not the kind of commercial, property, and other rights associated with investment enjoy parallel constitutional protection in a given State—which, for example, they generally do not in Canada.[139] He calls for investigating the regulatory chill impact of the North American Free

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subordinate bodies to enacts secondary legislation. This power is often viewed through the lens, and uses the language, of the United States, common-law *police powers* doctrine that protects regulatory measures from being subject to compensation under certain conditions. The regulatory power doctrine provides that a State possesses an inherent right to regulate in protection of the public interest and does not act wrongfully when, pursuant to this power, it enacts *bona fide*, non-discriminatory and proportionate regulations in accordance with due process. Thus, mostly it is defined as the capacity of States to regulate behavior and enforce order within their territory for the betterment of the health, safety, morals, and general welfare of their inhabitants. In Section 1.2.3, I explain how ISDS tribunals can limit the regulatory power of host States to protect the environment.

[136] Andrew Newcombe, "The Boundaries of Regulatory Expropriation in International law" (2005) 20:1 ICSID Review.

[137] Quoted in Hill, Jess, "ISDS: The Devil in the Trade Deal", ABC Radio National Australia (26 July 2015).

[138] David Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise* (Cambridge University Press, 2008) at 4.

[139] Ibid.

Trade Agreement **(**NAFTA) on certain branches of the Canadian government.[140] He shows the existence of the regulatory chill by referencing several ISDS cases that demonstrate the impact of NAFTA claims on the government's efforts in the public health sector.

To reaffirm this criticism, Van Harten and Scott conducted 51 interviews on whether the ISDS provision in NAFTA Chapter 11 contributed to a regulatory chill in the internal vetting of the government decisions related to environmental protection in Ontario.[141] They then report that "[g]overnment ministries have changed their decision-making to account for trade concerns including ISDS."[142] The federal government's proposals for plain cigarette packaging in Canada is an example that effectively shows the chilling effect of ISDS tribunals on Canadian regulatory sovereignty. In the mid-1990s, the US tobacco lobby threatened the Canadian government with an investor-state challenge to commence NAFTA arbitration proceedings if the Canadian government proceeded with planned restrictions on cigarette packaging. The federal government's proposals were abandoned and replaced with watered-down requirements to increase the size of health warning labels on packages. The foregoing example is provided both as a stark, easily understood instance and as an instance that shows chilling effects span the public health dimensions of sustainable development and not merely environmental protection in the strict sense.

For chilling effect examples with direct environmental impact, Van Harten and Scott note the following key cases: *Clayton/Bilcon v. Canada (2015)*[143] and *Windstream Energy v. Canada (2016).*[144] In the *Bilcon v. Canada* case, a U.S. company successfully challenged the rejection of its proposed quarry in Nova Scotia. After a preliminary approval of the project to develop and operate a quarry, a Joint Review Panel was mandated to conduct an environmental assessment. In

[140] The North American Free Trade Agreement (NAFTA) was a trade agreement between Canada, the United States, and Mexico, which came into force in 1994. In 2020, NAFTA was replaced by a modernized version called the United States–Mexico–Canada Agreement (USMCA). *United States–Mexico–Canada Agreement, U.S.–Mex.–Can., July 1, 2020*, online: <https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement>.

[141] Gus Van Harten & Dayna Nadine Scott, "Investment Treaties and the Internal Vetting of Regulatory Proposals: A Case Study from Canada" (2016) 7:1 Journal of International Dispute Settlement 92–116.

[142] *Ibid* at 93.

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[144] *Windstream Energy LLC v The Government of Canada (I),* Permanent Court of Arbitration (PCA) Case No 2013-22, Award 27 September 2016.

its final report, the Joint Review Panel recommended the rejection of the project. The significant and adverse environmental effect on the "community core values" were the main reason for the Joint Review Panel rejecting the project. The ISDS tribunal found that the review panel's decision, citing the project's negative impact on "community core values," was arbitrary and breached the investor's right to a minimum standard of treatment under NAFTA. While the company initially sought over $440 million in damages, the tribunal ultimately ordered the Canadian government to pay Bilcon $7 million plus interest, a significant penalty for implementing environmental protection law. Similarly, in the *Windstream Energy v. Canada* case stemming from Ontario's Green Energy Act, U.S.-based Windstream Energy was awarded millions after the provincial government implemented a sudden moratorium on offshore wind development, stalling the company's approved Lake Ontario project. The ISDS tribunal ruled that while the moratorium itself was a valid environmental policy, the government's unclear and scientifically unsupported implementation breached the minimum standard of treatment owed to the investor under NAFTA. The tribunal ordered Canada to pay Windstream $28 million in damages and legal costs. These decisions highlight a significant basis for a chilling effect, demonstrating that even well-intentioned environmental or energy policy shifts can be successfully challenged and prove costly if they are perceived as arbitrary or lacking in due process for foreign investors.

1.2.2.3 Levels of Compensation

The third corpus of criticism against ISDS tribunals is due to uncapped and non-appealable awards in favor of foreign investors that place huge, or at least potentially huge, burdens on host States' treasuries and thus on the economy more broadly. Every investor-state arbitration, regardless of sector or regulatory measures involved, has financial implications for host States. "The costs involved in defending an international arbitration are considerable … and if a tribunal finds against a state, the sums awarded may be significant."[145] Each dispute must, of course, be assessed based on its circumstances, but many countries have found themselves facing claims brought by foreign investors for millions, and sometimes billions, of US dollars. According to UNCTAD, up to the end of 2017, in cases decided in favor of the investor, the average amount

[145] Fiona Marshall & Howard Mann, "Good Governance and the Rule of Law: Express Rules for Investor-State Arbitration Required" (2006) International Institute for Sustainable Development Submissions at 3.

awarded to foreign investors per case was US$504 million, with an increase in extremely high-value cases.[146] For instance, in *Tethyan Copper v. Pakistan (2019)*,[147] the ISDS tribunal ordered Pakistan to pay more than US$ 5.9 billion in compensation, interest, and legal costs to Tethyan. In *Occidental v. Ecuador (2012),*[148] Ecuador was ordered to pay US$1.77 billion to the American oil company, Occidental. In this case, the ISDS tribunal largely awarded the investor without even considering whether the government of Ecuador would be able to compensate such a large award. Further, even when governments do not lose the disputes, they are often saddled with millions of dollars in fees and expenses from defending the cases. Thus, there is a constant and very real possibility that "states will shy away from the risk of costly and embarrassing arbitration when considering regulatory changes," particularly changes that might be seen as violating treatment standards included in IIA.[149]

This monetary punishment is decisive due to the lack of an appellate review of ISDS tribunals' decisions. Chung condemns the absence of an appeal mechanism and claims that it shocks the sense of the rule of law or fairness in the investment governance regime and impairs the legitimacy of ISDS tribunals.[150] Van Harten, in *Sovereign Choices and Sovereign Constraints*, emphasizes the far-reaching implications of ISDS tribunals' awards: "They order public compensation for investors, sometimes for vast amounts, and their awards—though largely and entirely beyond review by any court—are widely enforceable."[151] He argues that while ISDS tribunals are seen as a reciprocally consensual adjudication between investors and States, and while entering into an IIA treaty is an initial sovereign act of States including the host State later sued by an investor, there should be a mechanism of adjudicative review for resolving disputes arising from a sovereign act of host States. These shortcomings are magnified by the ISDS tribunals' power over public budgets by which awarded compensations can be paid out of the State's unprotected commercial assets in other countries through enforcement-of-award

[146] United Nations Conference on Trade and Development (UNCTAD), *Investor-State Dispute Settlement: Review of Developments in 2017* (2018).
[147] *Tethyan Copper Company Pty Limited v. Islamic Republic of Pakistan,* ICSID Case No ARB/12/1, Award 12 July 2019.
[148] *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador*, ICSID Case No. ARB/06/11, Award 5 October 2012.
[149] Bernasco Ni-osterwalder et al, *supra* note 29 at 14.
[150] Chung, *supra* note 126.
[151] Gus Van Harten, *Sovereign Choices and Sovereign Constraints: Judicial Restraint in Investment Treaty Arbitration* (Oxford: Oxford University Press, 2014) at 4.

proceedings.[152] Puvimanasinghe recapitulates these discontents and notes that the lack of right of appeal for high awards with strong enforcement measures generates severe challenges to the legitimacy of ISDS tribunals.[153]

1.2.3 Impeding Role of ISDS for Environmental Considerations

The general criticisms discussed in the above section push towards specific scrutiny about the conflicts that these tribunals can create between protecting foreign investors and safeguarding the environment in the host States. More specifically, in the context of environmental issues, these criticisms result in significant concerns that foreign investors could take advantage of ISDS tribunals to protect themselves to the detriment of the equally (or more) worthy goals of environmental protection. In practice, ISDS tribunals frequently render decisions that host States' environmentally-oriented regulatory actions "may constitute violations of applicable investment treaties, for which the State may be held internationally responsible and liable to provide sizable financial compensation to foreign investors."[154] Despite the fact that these measures were taken to fulfill host States' environmental obligations, foreign investors are allowed to challenge such measures before ISDS tribunals, as a result of which host States' conduct can be judged as expropriation or/and as an alleged violation of other IIA rules, in particular the fair and equitable standard, that consequently entitles foreign investors to monetary compensation.[155] For example,

[152] ISDS awards are enforced mostly in light of the ICSID Convention and the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. However, neither the ICSID Convention nor the New York Convention provides that States waive execution immunity by consenting to arbitration under it. State practice over the last several decades has shifted towards a restrictive theory of immunity with respect to assets subject to execution, meaning that government-owned assets in foreign States used for commercial purposes are not protected from execution by state immunity law. Thus, a successful investor might be able to execute his arbitral award against foreign commercial assets of a State.

[153] Puvimanasinghe, *supra* note 22 at 327.

[154] Klara Polackova Van der Ploeg, "Protection of Regulatory Autonomy and Investor Obligations: Latest Trends in Investment Treaty Design" (2018) 51:1 The International Lawyer 109–119 at 109.

[155] *Investor-State Dispute Settlement (ISDS) Mechanisms and the Right to a Clean, Healthy, and Sustainable Environment*, by David R Boyd (International Institute for Sustainable Development (IISD), Center for International Environmental Law (CIEL), and Clientearth, 2023). Although the dominant line of precedent in ISDS tribunals is to hold host States' legitimate environmental measures to be contrary to the FET standard, there are some cases in which investor protection has been subordinated to host States' right to adopt and enforce environment protection laws and measures, *David R Aven and Others v. Republic of Costa Rica,* ICSID Case No UNCT/15/3, Award 18 September 2018. For example, in *Aven v. Costa Rica*, the tribunal concluded that, under the applicable investment treaty, the rights of investors are subordinate to the right of Costa Rica to ensure that the investments are carried out "in a manner sensitive to environmental concerns," *Ibid* para 412. It also held that the host State had implemented and enforced its environmental laws "in a fair, non-discriminatory fashion, applying said laws to protect the environment, following principles of due process, not only for its adoption but also for its enforcement," *Ibid* para 413. Finally, the tribunal concluded that the measures undertaken by Costa Rica to protect the environment are

in 2022, the Italian government was ordered to pay compensation to UK oil company Rockhopper for an offshore oil drilling ban that was implemented for environmental protection concerns.[156] Rockhopper, a British oil company, had invested in an offshore oil project known as the Ombrina Mare field, located in the Adriatic Sea. In 2015, Italy introduced a law prohibiting oil and gas exploration and drilling within 12 nautical miles of its coast, effectively canceling Rockhopper's project. The company filed an ISDS claim, arguing that Italy's decision deprived it of its investment and violated its rights under the treaty. In August 2022, an arbitration tribunal ruled in favor of Rockhopper, determining that Italy's ban amounted to an expropriation of the company's investment. Italy was ordered to pay €191 million in compensation, significantly more than Rockhopper's initial investment of around €33 million. The compensation was based on the potential lost profits Rockhopper could have earned had the project proceeded.

This dynamic may bolster investors' ability to exert pressure on host States by leveraging the threat of investment arbitration to secure favorable settlements in environmental disputes.[157] The mere prospect of such disputes has become a powerful deterrent, discouraging host States from implementing regulatory measures that protect the environment but may negatively impact foreign investors. For instance, in 2017, the Canadian oil firm, Vermillion, threatened the French government with an ISDS case over its fossil fuel phase-out plan, ultimately leading to a weakened version of the environmental regulations.[158] Vermilion argued that the French government's proposed environmental law would violate its rights under the Energy Charter Treaty (ECT), an international agreement that protects energy investments. Vermilion claimed that the new law amounted to an indirect expropriation of its investments, as it would render its permits worthless, and that it was a breach of the treaty's fair and equitable treatment clause. Following Vermilion's legal threat and extensive lobbying, the French government passed a watered-down version of the law in late 2017. The final law, while still a step toward a fossil fuel

consistent with international law and neither arbitrary nor in breach of the obligations under the applicable investment treaty.

[156] *Rockhopper Exploration Plc, Rockhopper Italia S.pA and Rockhopper Mediterranean Ltd v. Italian Republic,* ICSID Case No ARB/17/14, Award 23 August 2022.

[157] "How Some International Treaties Threaten the Environment: Investor-State Dispute-Settlement Provisions are Blamed for Impeding Government Action", *The Economist* (2020), online: <https://www.economist.com/finance-and-economics/2020/10/05/how-some-international-treaties-threaten-the-environment>.

[158] *Investor–State Disputes in the Fossil Fuel Industry*, by Lea Di Salvatore (International Institute for Sustainable Development (IISD), 2021) online: <https://www.iisd.org/system/files/2022-01/investor–state-disputes-fossil-fuel-industry.pdf>.

phase-out, was significantly weakened: instead of a complete ban, the law allowed existing fossil fuel exploration and extraction permits to continue until their expiry, which in some cases could extend beyond 2040.[159]

Similarly, in 2022, both Denmark and New Zealand acknowledged that the fear of ISDS litigation had constrained their ability to implement climate policies within the investment sector.[160] A very important example of this dynamic in the Global South was Indonesia's decision to allow open-pit mining in protected forests following a threat of investment arbitration. Despite environmental concerns, the government's decision was taken under the profound influence of potential ISDS claims—in other words, this provides an example of regulatory chill where host States hesitate to enforce or enact environmental regulations due to fear of being sued before ISDS tribunals.[161] In 1999, Indonesia enacted Forestry Law No. 41, which prohibited open-pit mining in protected forest areas to safeguard the environment. This legislation affected numerous mining companies holding pre-existing contracts, leading to significant pushback from the industry. International mining corporations, notably Australia's Newcrest Mining, threatened to initiate arbitration before an ISDS tribunal, seeking substantial compensation for potential losses. These legal threats exerted considerable pressure on the Indonesian government, prompting it to relax the ban in 2004 by issuing a regulation that allowed 13 companies with prior contracts to continue their open-pit mining operations in protected forests.[162] This decision underscores how the threat of arbitration can compel governments to amend or revoke environmental protections, prioritizing investment interests over environmental consideration.[163]

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160 Elizabeth Meager, "Cop26 Targets Pushed Back under Threat of being Sued" (2022), online: *Capital Monitor* <https://capitalmonitor.ai/institution/government/cop26-ambitions-at-risk-from-energy-charter-treaty-lawsuits/>.

161 Kyla Tienhaara, "Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement" (2018) 7:2 Transnational Environmental Law 229–250.

162 Kyla Tienhaara, *The Expropriation of Environmental Governance: Protecting Foreign Investors at the Expense of Public Policy* (Cambridge University Press, 2009), 217–227; Stuart G Gross, "Inordinate Chill: BITS, Non-NAFTA MITS, and Host-State Regulatory Freedom-An Indonesian Case Study" (2003) 24 Michigan Journal of International Law 893.

163 The Swedish energy company Vattenfall and others brought a claim before an ISDS tribunal against Germany in relation to that country's recent decision to phase out nuclear power. The tribunal found that the Germany's phasing out of nuclear power decision amounted to a violation of the investors' legitimate expectations under the Energy Charter Treaty, and, therefore, the State should provide the company with appropriate monetary compensation, V*attenfall AB, Vattenfall Europe AG, Vattenfall Europe Generation AG v. Federal Republic of Germany (I),* ICSID Case No ARB/09/6, Award 11 March 2011. In *Vattenfall v. Germany*, Vattenfall, which had an agreement with the regional government of Hamburg, Germany, to develop a coal-fired power plant, commenced an investment treaty dispute due to Hamburg's environmental protection restrictions on its water-use permit. To settle the litigation,

Such chilling effects on States' regulatory power to implement measures intended to protect the environment obviously have significant impeding impacts on sustainable development. The recent report of *Investor-State Disputes in the Fossil Fuel Industry*, published in December 2021, reveals that the burning of fossil fuels is the primary driver of climate change, and, in response, policymakers worldwide are intensifying their actions to reduce emissions associated with fossil fuels.[164] For instance, the Paris Agreement, which is a legally binding international treaty on climate change adopted by 196 Parties in 2015, requires State parties to implement economic and social measures to end investments in fossil fuels.[165] Article 2.C. of the Paris Agreement states the objective of "making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development." This means that a substantial proportion of known fossil-fuel-dependent FDI projects would have to be left in the ground, and, very soon, host States will need to cut back on or prohibit further exploration activities in order to curtail fossil fuel extraction. In addition, other forms of implementation of policies and regulations related to the Paris Agreement, such as those targeting emission reductions or promoting renewable energy, can negatively affect FDI projects or their expected profits.

However, these actions might appear contrary to IIAs that were in existence before the imposition of the host State's environmentally-friendly investment requirements. For instance, measures taken to satisfy host States' obligations in accordance with the Paris Agreement could conflict with investment-protection standards whenever they ban the usage/production of various chemicals for environmental reasons,[166] refuse permits for hazardous waste landfill projects,[167]

Hamburg eased the environmental restrictions attached to the water-use permit. Some were of the view that this settlement effectively watered down German and European environmental law, demonstrating the regulatory chill effect in action, and led to popular calls for Germany to abandon its use of ISDS. See further and generally, Tienhaara, *supra* note 161.

[164] Di Salvatore, *supra* note 158.

[165] *Paris Agreement, U.N.T.S. Registration No. 54113, 12 December 2015 (entered into force 4 November 2016)*, online: <https://unfccc.int/sites/default/files/english_paris_agreement.pdf>.

[166] *Eco Oro Minerals Corp v. Republic of Colombia,* ICSID Case No ARB/16/41, Decision on Jurisdiction, Liability and Directions on Quantum 9 Sept 2021; *Infinito Gold Ltd v. Republic of Costa Rica,* ICSID Case No ARB/14/5, Award 3 Jun 2021.

[167] *Perenco Ecuador Limited v. Republic of Ecuador,* ICSID Case No ARB/08/6, Award 27 September 2019.

prohibit oil contamination,[168] forbid expropriation for reserves;[169] require environmental impact assessments,[170] alter incentives for renewable energies;[171] need phasing-out of nuclear and coal-fired power plants;[172] or prohibit conventional energy projects.[173] Such conflicts will then lead to investment disputes between foreign investors—bringing a claim before ISDS tribunals and arguing that the environmental measures taken by host States have violated investment protection provisions, most often the "fair and equitable treatment" standards—and host States who are parties to both the Paris Agreement and IIAs—defending their regulatory power with a public purpose and refusing investment treaties violations.[174] Regardless of who wins the case, such conflicts could impede the pace of sustainable development in host States.

These consequences stem from the inherently asymmetrical structure of ISDS tribunals, which have historically excessively empowered foreign investors by systematically prioritizing their rights over the regulatory autonomy of host States. As we have canvassed in this chapter, this arbitration framework is designed primarily to safeguard investor interests by granting foreign investors extensive legal protection rights against state actions while imposing little to no binding international obligations on investors, particularly concerning environmental responsibility and sustainable development. This imbalance presents significant challenges, as it effectively shields investors from accountability for environmental harm while restricting the ability of host States

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[168] *Burlington Resources, Inc v. Republic of Ecuador,* ICSID Case No ARB/08/5, Award 7 February 2017.
[169] *Compañia del Desarrollo de Santa Elena SA v. Republic of Costa Rica,* ICSID Case No ARB/96/1, 17 February 2000; *Marion Unglaube v. Republic of Costa Rica,* ICSID Case No ARB/08/1, Award 16 May 2012.
[170] *Emilio Agustín Maffezini v. The Kingdom of Spain,* ICSID Case No ARB/97/7, Award 13 November 2000.
[171] *Cavalum SGPS, SA v. Kingdom of Spain,* ICSID Case No ARB/15/34; *Abengoa, S.A. and COFIDES, S.A. v. United Mexican States,* ICSID Case No. ARB(AF)/09/2, Award 18 April 2013; *Quiborax SA, Non-Metallic Minerals SA v. Plurinational State of Bolivia,* ICSID Case No ARB/06/2, Award 16 September 2015; *Latam Hydro LLC and CH Mamacocha SRL v. Republic of Peru,* ICSID Case No ARB/19/28, Award 20 December 2023.
[172] *Vattenfall AB and Others v. Federal Republic of Germany (II),* ICSID Case No ARB/12/12; *Westmoreland Mining Holdings, LLC v. Government of Canada,* ICSID Case No UNCT/20/3, Award 31 January 2022.
[173] *Rockhopper Exploration Plc, Rockhopper Italia S.pA and Rockhopper Mediterranean Ltd v. Italian Republic,* ICSID Case No ARB/17/14, Award 23 August 2022; *Lone Pine Resources Inc v Canada,* ICSID Case No UNCT/15/2, Award 21 November 2022.
[174] *Climate Change and International Investment Agreements: Obstacles or Opportunities?*, by Fiona Marshall (International Institute for Sustainable Development (IISD), 2010) at 35. Tienhaara and Cotula point out that 75% of the foreign-owned coal power plants that need to be retired early in line with the Paris Agreement are covered by at least one IIA which includes ISDS tribunals, *Raising the Cost of Climate Action? Investor-State Dispute Settlement and Compensation for Stranded Fossil Fuel Assets*, by Kyla Tienhaara & Lorenzo Cotula (International Institute for Environment and Development (IIED), 2020) online: <https://www.iied.org/17660iied>. See also *Investor–State Disputes in the Fossil Fuel Industry*, by Lea Di Salvatore (International Institute for Sustainable Development (IISD), 2021) that notes the number of fossil fuel cases in the ISDS tribunals has been increased when phasing out fossil fuels is imperative to comply with the Paris Agreement's objectives.

to implement or enforce environmental regulations without the risk of costly arbitration claims—especially when States are aware that the basis for calculating compensation can extend to loss of future profits (recall *Rockhopper* as one example). As a result, States may be deterred from pursuing necessary environmental policies due to the ever-looming threat of investor-state disputes exacerbating the global struggle to achieve SDGs.

In this context, the *ICSID's Biannual Caseload Statistics* report indicates that parallel with the intensified actions of States towards climate change management, ISDS tribunals have been utilized more and more often by foreign investors in the fossil fuel sector to challenge the environmental measures taken by host States.[175] This data is confirmed by case-related trends in the 2023 fiscal year that show foreign investors in the fossil fuel industry are at the forefront of extensively utilizing the ISDS tribunals for investment protection by impeding the progress and adoption of initiatives aimed at addressing climate change, posing significant challenges for host States aspiring to transition away from fossil fuels. It is worth quoting here several major findings of the *Statistics* report:

> A full range of economic sectors are involved in ICSID cases. As in previous years, the extractives and energy sectors accounted for the largest share of cases in FY2023. Twenty-seven percent of new cases involved the oil, gas, and mining industry and 15% related to electric power and other energy sources. The finance sector was also prominent, accounting for 11% of cases. Construction and transportation each made up 9%, while information and communication, and agriculture, fishing, and forestry each accounted for 7%. Other cases involved water, sanitation, and flood protection (4%); tourism (2%); and services and trade (2%). A mix of other industries accounted for the remaining 7% of cases registered in FY2023.[176]

The outcomes of these disputes are in the hands of ISDS tribunals who have to determine whether measures taken by host States in accordance with the Paris Agreement or any other environmental policies have indirectly expropriated FDI projects and constituted a violation of IIAs' obligations and, thus, whether host States are obliged to compensate foreign investors. Despite the importance of sustainable development goals, data shows that ISDS tribunals are often reluctant to consider environmental purposes when drawing a line between compensable and non-compensable measures taken by host States. According to the 2021 *Investor-State*

[175] International Centre for Settlement of Investment Disputes (ICSID), *supra* note 63.
[176] *Ibid*.

Disputes in the Fossil Fuel Industry report, the share of ISDS tribunals decided in favor of the investor rises sharply in fossil-fuel-related disputes. It reports that "[out] of the 60 disclosed arbitral awards, only 13 were decided in favour of the State based on the merits, while 43 have been decided in favour of the investor, which corresponds to over 70% of total disclosed fossil fuel arbitrations. In other words, of the fossil fuel arbitrations that reach the merits stage, almost three out of four are decided in favour of the investor."[177] The *ICSID's Biannual Caseload Statistics: 2023-2* report also reveals that among cases decided by tribunals in FY2023, 59% of awards upheld the investors' claims in part or in full, 24% of awards rejected all of the investors' claims on the merits, 14% of awards declined jurisdiction, and 3% of awards decided that the claims are manifestly without legal merit.[178] Therefore, decisions of ISDS tribunals that are made in favor of investment protection and oblige host States to pay compensation could create a situation where States become torn between maintaining the conditions that were conducive to attracting foreign investors (allowing the continuous operation of fossil fuel-dependent FDI projects) and compensating damages caused by new environmentally-related measures (in the climate context, implementing the Paris Agreement's environmental measures). To reiterate once more for emphasis, this can induce regulatory chill in host States towards advancing their sustainable development goals.

1.2.3.1 Sole Effect Doctrine, Regulatory Power Doctrine, and Investment Reprisal Approach

The impeding role of ISDS tribunals for the *2030 Agenda for Sustainable Development* has been at the centre of critical legal scholarship in the field. Scholars note that whether by their operation or threatened invocation, ISDS tribunals "[have] raised issues concerning a State's ability to regulate its affairs, particularly in important areas such as the environment or social policy."[179] Legal scholars then discuss these issues through the two aspects of ICSID tribunals: ideological underpinnings and institutional framework.[180]

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[177] Di Salvatore, *supra* note 158 at 16.
[178] International Centre for Settlement of Investment Disputes (ICSID), *supra* note 63.
[179] Nelson Goh, "ESG and Investment Arbitration: A Future with Cleaner Foreign Investment?" (2022) 15 Journal of World Energy Law and Business 485–501 at 485.
[180] Scholars who criticize ISDS tribunals under ICSID Convention include but are not limited to Sornarajah, *supra* note 122; Christoph Schreuer, *The ICSID Convention: A Commentary*, 2nd edn (Cambridge: Cambridge University Press, 2009); Van Harten, *supra* note 151; Karl P Sauvant & Federico Ortino, *Improving the International Investment Law and Policy Regime: Options for The Future* (Minister for Foreign Affairs of Finland, 2013); Viñuales, *supra* note 100.

Initiating with the ideological underpinnings, legal scholars question the location of ISDS tribunals in global and interstate power relations. They claim that the current discontent over the incompatibility of ISDS tribunals with the environmental aspect of sustainable development stems from a long-term history of inequality between developed and developing countries in international lawmaking that continues to affect the ICSID Convention.[181] The World Bank sponsors a unitary system of principles via the ICSID Convention aimed at protecting foreign investors whose home States are primarily developed countries with little formal room for safeguarding the natural environment of host States, the majority of which are developing countries.[182] Moreover, since investors from high-income States typically initiate ISDS claims,[183] "an uncomfortable reality may come into existence wherein investors from the wealthiest states challenge policies of low-income states designed to alleviate the impacts of climate change on that state."[184] Therefore, the ISDS tribunals primarily invented to protect the West's economic control of the world in the decades following decolonization are now bulwarks against developing countries' attempts to protect their environment.[185] Even if one were to hold out hope by virtue of more recent IIAs that mention sustainable development, developed countries continue to have more experience and diplomatic-legal resources in negotiating and drafting IIAs, which can easily result in the same tradition of more robust protections for investors over other important societal matters and concerns, including the environment of developing countries not to mention the environment of the Earth as a whole.[186]

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[181] Islam, *supra* note 60.
[182] Mann & Von Moltke note that "existing IIAs have not been designed to meet the development needs of developing countries, let alone to promote sustainable development globally," Howard Mann & Konrad Von Moltke, *NAFTA's Chapter 11 and the Environment: Addressing the Impacts of the Investor-State Process on the Environment* (International Institute for Sustainable Development, 1999) at 20.
[183] United Nations Conference on Trade and Development (UNCTAD), *Investor-State Dispute Settlement Cases Pass the 1,000 Mark: Cases and Outmarks in 2019* (2020).
[184] Amanda Lees et al, "Suitability of ISDS for Societal Challenges" (2022) Global Arbitration Review, online: <https://globalarbitrationreview.com/guide/the-guide-investment-treaty-protection-and-enforcement/first-edition/article/suitability-of-isds-societal-challenges>.
[185] *Environmental Concerns in International Investment Agreements: A Survey*, by Kathryn Gordon & Joachim Pohl (OECD Working Papers on International Investment, 2011).
[186] Jose E Alvarez, "ISDS Reform: The Long View" (2021) 36:2 ICSID Review - Foreign Investment Law Journal 253–277; Gleason, *supra* note 2.

Most importantly, legal scholars continue their discussion by challenging the institutional framework of ISDS tribunals that essentially prioritize pro-investment provisions included in IIAs over host States' environmental regulations.[187] Institutional actors like the United Nations Environment Programme also raise this concern. The UNEP draws attention to how ISDS tribunals are currently and will continue to be used by foreign investors to challenge legitimate environmental measures of host States:

> One of the main concerns underlying this [ISDS tribunals] is that foreign investors have used the system to seek excessive protection against normal and legitimate regulatory change. Legitimate environmental measures, such as the creation of a natural preserve, the non-renewal of environmental permits, the phasing out or the prohibition of harmful chemical substances, requirements of land decontamination, liability actions for environmental pollution, and many other similar measures have been challenged by foreign investors as a violation of investment protection standards.[188]

This highly controversial practice of ISDS tribunals that thwarts and/or weakens many host States' meaningful actions towards environmental protection is often due to the widespread application of the *sole effects doctrine*,[189] the restricted utilization of the *regulatory power doctrine*,[190] and the infrequent recourse to the *investment reprisal approach*[191] used by investment arbitrators in investor-state disputes.

1.2.3.1.1 Overview of ISDS Tribunals' Practice

The sole effect doctrine prioritizes the effect of State measures on the economic interests of foreign investors over effects of measures on the environmental objectives of host States, both when characterizing State conduct (is it expropriatory? is it unfair?) and when determining extent of compensation. Another way of putting it is that the sole effect doctrine underpins ISDS tribunals' adoption of a narrow approach to what the purpose of IIAs is (protecting economic investment), what interests are protected by IIAs (investors), and to whether and how purposes extraneous to international investment law should be systemically considered in reading IIA

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[187] For instance Van Harten notes that "[investment] arbitration arbitrators have emerged as potential overseers of all other entities by which sovereignty is exercised," Van Harten, *supra* note 151 at 4.
[188] at 12.
[189] Ben Mostafa, "The Sole Effects Doctrine, Police Powers and Indirect Expropriation under International Law" (2008) 15:1 Australian International Law Journal 267–296.
[190] Jimena Sierra-Camargo & Federico Suárez-Ricaurte, "The Right to Regulate" in David Schneiderman & Gus Van Harten, eds, *Rethinking Investment Law* (Oxford University Press, 2023) 180.
[191] Martin Jarrett, *Contributory Fault and Investor Misconduct in Investment Arbitration* (Cambridge: Cambridge University Press, 2019).

texts. The result is ISDS tribunals emphasizing that they may only consider the extent to which the conduct of the host State violates its obligations under a specific IIA (as understood within a web of international investment law doctrine arising from other IIA/ISDS arbitrations) and then going on to hold that host States must compensate foreign investors fully.

Conversely, the regulatory power doctrine seeks to widen the lens on relevant effects. This doctrine gives weight to the environmental regulatory power of host States in pursuit of beneficial environmental impacts and considers the negative effects of the environmentally risky performance of foreign investors. With respect to claims of indirect expropriation, this doctrine permits analysis of the State's motives such that good faith efforts to regulate for the environmental public interest can be taken into account in characterizing whether the State measures are in fact expropriation or are in fact legitimate regulation. Especially with respect to the fair and equitable treatment standard, a form of balancing analysis is carried out whereby, if legitimate use of regulatory power is found, then no breach of the IIA occurs and thus no compensation is owed to the foreign investor claiming injury. That analysis "weighs the public purpose of the measure against the burden placed on the investor and requires there be a reasonable relationship of proportionality."[192] As this approach posits that the purpose of the measure taken by host States and the foreign investors' actions that motivated such measures may all be relevant to the indirect expropriation question and compensation assessment, it faces serious challenges being recognized in the current investment dispute jurisprudence dominated by the assumptions and approach of the sole effect doctrine—and in light of the alternative, less-all-or-nothing path of the investment reprisal approach discussed next.

The investment reprisal approach is a more moderate strategy as compared to the regulatory power doctrine, and, on a continuum, could be placed between the sole effect doctrine and the regulatory power doctrine. Like the regulatory powers approach, this approach considers both financial burdens imposed on foreign investors as a result of measures taken by host States and the environmental objectives behind (and effects of) the measures. However, if the analysis results in a finding that an investment protection standard has been breached (notably, because

[192] *Climate Change and International Investment Agreements: Obstacles or Opportunities?*, by Fiona Marshall (International Institute for Sustainable Development (IISD), 2010) at 44.

the burden on the investor is viewed to be disproportionate even if the measures are otherwise found to be a legitimate and sufficiently targeted response to harms caused by investors), the investment reprisal approach rejects the either/or approach to compensation of both the sole effect doctrine and regulatory power doctrine. Accordingly, host States are responsible for partially, not fully, compensating foreign investors whose environmentally harmful and/or risky activities have motivated host States to take measures that adversely affect their investments. It may be that an arbitrator employing this approach is more likely to give greater weight to the burden placed on the investor than a full-bore regulatory powers analysis would—precisely because the tribunal would know contextualized justice can still be done at the compensation stage. While the sole effect doctrine is predominant by far, and the regulatory power doctrine infrequently results in a favourable outcome for States, the investment reprisal approach seems to be gaining favour.

1.2.3.1.2 The Sole Effects Doctrine

The sole effects doctrine, which is the most common perspective invoked in investment law jurisprudence, suggests ISDS tribunals should primarily or exclusively consider the impact of a disputed measure on investment when evaluating claims of indirect expropriation or violation of any treatment standards included in IIAs. According to this doctrine, other factors, such as the government's intention or the purpose of the measure, should not be given significant consideration in assessing an indirect expropriation claim. This doctrine considers the purpose of regulatory measures taken by host States irrelevant and notes that the only thing that matters in evaluating whether host States have indirectly expropriated foreign investments "is the extent of the measure's impact on the investor."[193] The sole effects doctrine applied by ISDS tribunals is not just a kind of legalistic reductionism but also justifies itself with value-laden purposive arguments. One basis for the doctrine is the assumption that IIAs are geared towards protecting against the expropriation measures of host States, and thus, any doubt as to whether a measure or regulation amounted to expropriation ought to be resolved in favor of the investor.[194] Therefore, ISDS tribunals embrace the sole effects doctrine as more consistent with IIAs' pro-investment

[193] *Ibid*.
[194] Virtus Chitoo Igbokwe, "Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations" (2006) 23:4 Journal of International Arbitration 267.

nature and objects,[195] apart from (returning to the mention of reductionism) also relying on a single criterion of economic effects because this makes assessment simpler and more predictable.[196]

The use of the sole effects doctrine in assessing claims for IIAs violations is thus one reason investment tribunals pay little attention to the environmental purpose of measures taken by host States when deciding whether damages imposed on foreign investors are compensable or non-compensable.[197] While the sole effects doctrine has been commonly invoked in investment law jurisprudence, it has been challenged by a number of ISDS decisions that argue the necessity of considering host States' intention behind regulatory measures alleged to be indirect expropriation. Taillant and Bonnitcha discuss how the sole effects doctrine is an unreasonable but dominant approach according to which "[ISDS] tribunals have prioritized States' obligations under applicable investment regulation" and give a constrained scope to the welfare regulatory obligations held by States.[198] With such a dominant approach, host States have no choice but to comply with their obligations under IIAs, and "if the host state measures substantially impact the property of foreign investors or its use, they may constitute a compensable expropriation."[199] Cordonier Segger and Newcombe also observe that, in cases where new environmental regulations are necessary for the public interest, "the decisions of IIA tribunals have favored foreign investors to the detriment of [the environment of] host States."[200] They argue that ISDS tribunals have been biased in favor of investment protection while neglecting the nature, purpose, and character of the measures taken by host States. In only considering measures' effect on investors' use of their property,[201] ISDS tribunals "reduce the regulatory space available to host

[195] Mostafa, *supra* note 189 at 267.
[196] Lukas Vanhonnaeker, *Intellectual Property Rights as Foreign Direct Investments: From Collision to Collaboration* (United Kingdom: Edward Elgar Publishing, 2015) at 44.
[197] Jorge E Viñuales, "The Environmental Regulation of Foreign Investment Schemes under International Law" in Pierre-Marie Dupuy & Jorge E Viñuales, eds, *Harnessing Foreign Investment to Promote Environmental Protection Incentives and Safeguards* (Cambridge: Cambridge University Press, 2013) at 4.
[198] Jorge Daniel Taillant & Jonathan M Bonnitcha, "International Investment Law and Human Rights" in Marie-Claire Cordonier Segger, Markus Gehring & Andrew Newcombe, eds, *Sustainable Development in World Investment Law* (Kluwer Law International, 2011) at 56.
[199] Zagel, *supra* note 96 at 29.
[200] Cordonier Segger & Newcombe, *supra* note 90 at 103.
[201] Attila Tanzi, "On Balancing Foreign Investment Interests with Public Interests in Recent Arbitration Case Law in the Public Utilities Sector" (2012) 11:1 The Law & Practice of International Courts and Tribunals 47 at 48.

countries to adopt measures in the public interest."[202] Accordingly, whatever other rules or principles of general international law tribunals are permitted to draw upon in their reasoning, more specific international environmental laws in light of which host States have taken environmental measures are denied as a route for justifying the non-compensatory nature of their exercise of regulatory power.[203] It then induces host States not to protect their natural environment when they have been threatened with foreign investors' claims before ISDS tribunals.

1.2.3.1.3 Regulatory Power Doctrine

In contrast to the sole effect doctrine, the regulatory power doctrine "has some promise to balance a system that emerged, originally, to protect and privilege foreign investors in a (post-) colonial context."[204] Sovereign states have inherent power to regulate in the public interest and this regulatory power has been recognized as a rule of customary international law.[205] In investment disputes whereby host States adopt measures which are in the public interest but adversely affect investors' private interests, ISDS tribunals could choose to apply the regulatory power doctrine to decide that host States need not compensate investors in circumstances that might otherwise amount to violations of a treaty. In this approach, ISDS tribunals intend to draw a distinction between non-compensable acts adopted by the State in the pursuit of legitimate public welfare purposes and acts not in the public interest that require the payment of compensation. [206] The regulatory power doctrine constitutes a full substantive defence to claims of indirect expropriation or/and fair and equitable treatment standards—with the result that no breach of the IIA is found and, thus, no compensation is due.

It is especially with respect to indirect expropriation that there is a presumption against the finding of an indirect expropriation in cases in which regulatory power is exercised.[207] Regulatory power doctrine explains a State is not liable for its *bona fide* regulations which could

[202] Prabhash Ranjan, "Police Powers, Indirect Expropriation in International Investment Law, and Article 31(3)(c) of the VCLT: A Critique of Philip Morris v. Uruguay" (2019) 9:1 Asian Journal of International Law 98–124 at 123.
[203] See thereby the ISDS tribunal looked to substantive norms beyond the investment field.
[204] Sierra-Camargo & Suárez-Ricaurte, *supra* note 190 at 180.
[205] Jeremy Waldron, "Are Sovereigns Entitled to the Benefit of the International Rule of Law?" (2011) 22:2 European Journal of International Law 315–343.
[206] Lone Wandahl Mouyal, *International Investment Law and the Right to Regulate: A Human Rights Perspective* (Taylor & Francis, 2016).
[207] Sierra-Camargo & Suárez-Ricaurte, *supra* note 190.

not constitute an indirect expropriation.[208] However, there is "no guidance that arbitral tribunals in distinguishing such actions from regulatory measures not subject to compensation."[209] This results in inconsistency in ISDS tribunals' decisions when they apply the regulatory power doctrine to the extent that, in some cases, they relieved States from the duty to compensate investors where regulation has a legitimate public purpose,[210] while in others, they have held the State to a much harsher standard.[211]

In the context of the fair and equitable treatment standard, the regulatory power doctrine requires a balance between foreign investors' financial interests and host States' public interests. However, the fair and equitable treatment standard has a number of sub-standards, such as when foreign investors claim denial of justice and full protection, which are not subject to any exceptions and from which no derogations are permitted, the regulatory power doctrine cannot exonerate host States from compensating foreign investors. In such cases, ISDS tribunals have often reduced the scope of state regulatory authority to favour investors.[212] Accordingly, despite the potential of the regulatory power doctrine to preserve regulatory space and rebalance the inequities of ISDS, the wide margin of interpretation and ambiguity of indirect expropriation and the fair and equitable treatment standards allow legitimate expectations of investors to displace host States' regulatory purposes such as responsiveness to environmental concerns.

1.2.3.1.4 Investment Reprisal Approach

The investment reprisal approach, similar to the regulatory power doctrine, is a relatively more balanced approach that not only weighs the environmental motivations behind the measures taken by host States but also considers the financial effects of the measures on foreign investors in order to reduce damage compensation in investment disputes. When the environmentally risky activity of the foreign investor breaches the host State's environmental rights, the injured host State adopts an environmental measure in response to that investor activity that the investor

[208] *Ibid*.
[209] Vera Korzun, "The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs" (2017) 50 Vanderbilt Journal of Transnational Law 355 at 375.
[210] *Philip Morris Brands Sàrl, Philip Morris Products SA and Abal Hermanos SA v. Oriental Republic of Uruguay,* ICSID Case No ARB/10/7, Award 8 July 2016.
[211] *Tecnicas Medioambientales Tecmed SA v. The United Mexican States,* ICSID Case No Arb (AF)/ 00/2, Award 29 May 2003.
[212] Daria Davitti, "Proportionality and Human Rights Protection in International Investment Arbitration: What's Left Hanging in the Balance?" (2020) 89 Nordic Journal of International Law 343.

argues violates its investment protection rights. In such a case, if the foreign investor challenges the legitimacy of the measure under the indirect expropriation standard, the ISDS tribunal could apply the investment reprisal approach to determine that, while the host State's measure does breach an IIA standard, the breach is nonetheless only partially compensable in light of the environmental motivation behind its measure along with the measure being sufficiently tailored to be the specific reprisal it claims to be. Thus, the notion of investment reprisal, as conceived by Jarrett, conveys the concept that, while "some blameworthy conduct performed by the investor …provokes the host State's breach [of an IIA]," the blameworthiness may serve as a defence that reduces host States' accountability towards injured investors.[213] It might this be said that an investment reprisal is permissible, although not substantively lawful, in the sense of qualifying the extent of wrongfulness with the normative work being done at the stage of apportioning fault and determining quantum of compensation.

In contemporary legal practice, the notion of investment reprisal risks carrying the connotation of a lawful "countermeasure" in the general public international law sense (where peaceful reprisal and peaceful countermeasure are often used interchangeable as terms). By the law of countermeasures, properly invoked and maintained countermeasures are a "circumstance precluding wrongfulness" where the lawfulness arises from the measure being a proportionate response to another State's wrongdoing, with the goal of coercing the State to stop that wrongdoing (at which point the countermeasure is also supposed to end).[214] "Reprisal" as used in the international investment law realm shares the idea of a response to a prior legal wrong of some sort, but it does not make the State's response lawful. Nor does the investment reprisal operate analogously to the regulatory power—which, if a legitimate exercise of such power is found, is a full defence against wrongfulness. Instead, the legitimacy of the investment reprisal influences the determination of compensation for the investor and can result in reducing damages that should be paid by host States to foreign investors.[215]

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[213] Jarrett, *supra* note 191 at 110.
[214] International Law Commission (ILC), *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries* (2001), online: <https://legal.un.org/ilc/texts/instruments/english/commentaries/9_6_2001.pdf> Article 22.
[215] Barnali Choudhury, "Recapturing Public Power: Is Investment Arbitration's Engagement of the Public Interest Contributing to the Democratic Deficit?" (2008) 41:3 Vanderbilt Journal of Transnational Law 775.

Investment reprisal can partly be derived from Article 39 of the International Law Commission (ILC) Draft Articles on Responsibility of States for Internationally Wrongful Acts.[216] Article 39, on contributory fault, says: "In the determination of reparation, account shall be taken of the contribution to the injury by willful or negligent action or omission of the injured State or any person or entity in relation to whom reparation is sought." This article notes that a victim's willful or negligent conduct that has materially contributed to the injury caused by an internationally wrongful act should be taken into account when determining compensation. This concept of contribution initially emerged in the context of inter-state relations (although a concept like contributory fault is also arguably a general principle of law applicable to all legal relations, whether between States, between individuals, or between States and individuals), but it has then percolated into international investment law whereby investment arbitrators have increasingly relied upon it to reduce the loss suffered by investor if the foreign investors were also at fault.

However, despite the potential of the investment reprisal approach to partially validate host States' environmental measures that still constitute investment treaty violations, there are compelling reasons why ISDS tribunals have limited their acceptance of the dispute settlement procedures. First, investment reprisal should only apply in circumstances where the host State has no other course of action available to it in pursuing justice for the investor's illegality. Thus, if there is another avenue for seeking justice against the relevant wrongdoer, ISDS tribunals reject the application of the investment reprisal approach. Second, considering the exceptional nature of investment reprisal as a permitted form of self-help, it should only apply in circumstances where the investor's misconduct is particularly egregious, which will not usually be the case with mere breaches of domestic law.[217] Third, the investment reprisal approach is, to date, being accepted in ISDS tribunals only in indirect expropriation cases. If an investor is denied fair and equitable treatment, national treatment, or most-favored nation treatment, the State cannot justify its actions through investment reprisal.[218] In particular, due to the multiple possible bases for investor protection under the fair and equitable treatment standard and with all of them focused at some

[216] International Law Commission (ILC), *supra* note 214.
[217] Jean-Michel Marcoux & Andrea K Bjorklund, "Foreign Investors' Responsibilities and Contributory Fault in Investment Arbitration" (2020) 69:4 International & Comparative Law Quarterly 877–905.
[218] Choudhury, "Recapturing Public Power", *supra* note 215 at 793.

level on *illegitimate* conduct, justifying host States' environmental regulatory measure as a *legitimate* reprisal is so far a bridge too far for tribunals.[219] As a result of the reprisal defence being rejected or circumvented, host States are found liable to compensate foreign investors without taking into account any contributory fault of the investor.

1.2.3.2 Case Law

In this section, I analyze how the ICSID tribunal, in the *Metalclad (2000)*, applied the sole effect doctrine to protect only investors' rights without considering the environmental motivations behind the measures taken by the host State. In *Metalclad*, despite the host State's environmental concerns, the ISDS tribunal decided that the host State must fully compensate the foreign investor.

Philip Morris (2016) is the second case that I analyze to explain how the regulatory power doctrine can be applied in the ISDS tribunal to exonerate the host State from compensating the foreign investor. In this case, although the regulatory measures taken by the host State adversely affected the foreign investors, their public purposes made the measures non-compensable. To indicate the restricted utilization of the regulatory power doctrine, I also discuss the *Azurix (2006)* case. In that case, the ISDS tribunal started out by indicating its willingness to give weight to the environmental motivation behind the measures in order to consider them as a legitimate regulatory act of the host State. However, the tribunal still found the measures unfair and inequitable and thus held the host State responsible to compensate the investor.

I then analyze the *Copper Mesa (2016)* case wherein, by relying on Article 39 of the ILC Articles on State Responsibility, the ISDS tribunal decided that the investor's injury was caused both by the host State's unlawful expropriation and also by the investor's own contributory negligent acts. In this case the ISDS tribunal applied the investment reprisal approach to reduce compensation costs.

[219] Marshall, *supra* note 192.

1.2.3.2.1 The Metalclad Case

Metalclad v. Mexico is a high-profile case that encapsulates the sole effect doctrine because the ISDS tribunal took the view that the purpose of a measure depriving an investor of the benefit of its investment is irrelevant to whether or not the measure may amount to expropriation.[220] In this case, the ISDS tribunal considered solely the economic effect of the measures taken by the host State on the foreign investors while sidelining the host State's environmental motivations and awarded the host State to fully compensate the foreign investor. This economic impact test provides a very stark test for an expropriation that would capture virtually every type of environmental protection measures which, at least in the short term, impose some costs or limit some economic benefit of a business. Thus, despite acknowledging the importance of environmental motivations behind the measures taken by the host State, the ICSID tribunal applied the sole effect doctrine and characterized the host State's measures as expropriation.

Metalclad Corporation v. The United Mexican States

In 1993, Metalclad entered into an agreement with the Mexican government to acquire COTERIN, a hazardous waste transfer station. This acquisition was based on a permit issued by the state government to extend a land use authorization for a hazardous waste landfill. However, shortly after Metalclad purchased COTERIN, the state governor initiated a campaign against the landfill. In December 1995, the municipality rejected Metalclad's application for a landfill construction permit. Finally, in 1997, the state governor issued an Ecological Decree designating the property as a Natural Area to protect rare cacti. This decree effectively prohibited Metalclad from utilizing its facility, akin to establishing a nature reserve or park.

Taken together, these events formed the basis of Metalclad's initial complaint before the ICSID tribunal. Metalclad's allegations in the NAFTA dispute centered around three violations of the agreement. First, Metalclad claimed that the sequence of actions resulting in

[220] *Metalclad Corporation v. The United Mexican States,* ICSID Case No. ARB(AF)/97/1, Award 30 August 2000, *supra* note 167.

the denial of the construction permit and the inability to operate the hazardous waste landfill violated NAFTA's Article 1105 on the Minimum Standard of Treatment standard. Second, Metalclad argued that these same actions constituted an indirect expropriation under NAFTA's Article 1110 on the Expropriation and Compensation standard. Finally, Metalclad contended that the Ecological Decree itself was a breach of NAFTA's Article 1110 on the Expropriation and Compensation standard.

The tribunal ruled in favor of Metalclad on all three claims and awarded the company damages of $16.5 million, which represented the amount of its lost investment costs. Regarding the first issue, the tribunal held that Article 1105 requires the host state to ensure "that all relevant legal requirements for the purpose of initiating, completing and successfully operating investments made, or intended to be made, under the agreement should be capable of being readily known…. There should be no room for doubt or uncertainty on such matters. Once the authorities of the central government of any Party… become aware of any scope for misunderstanding or confusion in this connection, it is their duty to ensure that the correct position is promptly determined and clearly stated so that investors can proceed with all the appropriate expedition in the confident belief that they are acting in accordance with all relevant laws."[221] Thus, in the absence of any clear rule on the need or process for obtaining a construction permit in the municipality, "Mexico failed to ensure a transparent and predictable framework for Metalclad's business planning and investment" and constituted a breach of Article 1105.[222]

In relation to the series of events leading to the denial of the construction permit and the issuance of the Ecological Decree, the tribunal held that the government effectively and unlawfully prevented the operation of the landfill, in a manner that amounted to expropriation in breach of Article 1110. The critical issue in this decision is how the tribunal used a test that focuses on the economic impacts of the measures and the protection of the investors' expectations to establish whether an expropriation had taken place. On the expropriation issue, the tribunals noted, "expropriation under NAFTA includes not only open, deliberate and

[221] *Ibid* para 76.
[222] *Ibid* para 99.

acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favor of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State."[223]

The tribunal decided the matter based solely on the denial of the construction permit, but went on to comment (in *obiter*, as it were) that the singular economic impact test as the primary test for expropriation would also have decided the matter if they had needed to consider the Ecological Decree as well. The tribunal stated that it "need not decide or consider the motivation or intent of the adoption of the Ecological Decree" and "an expropriation finding on the basis of the Ecological Decree is not essential to the tribunal's finding of a violation of NAFTA Article 1110." But it made clear what the result would have been: "However, the tribunal considers that the implementation of the Ecological Decree would, in and of itself, constitute an act tantamount to expropriation."[224]

1.2.3.2.2 The Philip Morris Case

Quite contrary to the *Metalclad* case, in *Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v. Oriental Republic of Uruguay*, the ISDS tribunal affirmed the regulatory power doctrine and rendered the measures taken by the host State non-compensatory.[225] In this case, the ISDS tribunal found that the measures were in exercise of Uruguay's sovereign right to regulate public health; considering the burden generated for the investor by any degree of economic impact is not part of the regulatory power doctrine. This award found that Uruguay's laws did not expropriate the foreign investors or constitute a breach of Uruguay's obligation to provide the foreign investor with fair and equitable treatment under the Switzerland-Uruguay BIT. The ISDS tribunals upheld Uruguay's sovereign power to regulate public health over Philip Morris's investment claims.

[223] *Ibid* para 103.
[224] *Ibid* para 111.
[225] *Perenco Ecuador Ltd. v. Republic of Ecuador and Empresa Estatal Petróleos del Ecuador,* ICSID Case No. ARB/08/6, Award 8 July 2016, *supra* note 210.

Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v. Oriental Republic of Uruguay

In 2008, the government of Uruguay passed a Single Presentation Requirement regulation to control the smoking rate in the country. This anti-smoking policy instrument provides that tobacco manufacturers could no longer sell multiple varieties of their brand. It also required health warnings to be printed on 50 per cent of the area of cigarette packages. One year later, in 2009, the second measure concerned the so-called "80/80 Regulation" was passed by the government. Under a 2009 presidential decree, the health warnings were to cover 80 per cent, instead of 50 per cent, of the packaging. This meant that only 20 per cent was left for the tobacco companies' trademarks and other information. As a result of these regulations, Abal Hermanos S.A., Philip Morris Brands Sàrl and Philip Morris Products S.A. (Philip Morris), whose main activity has been the importation of cigarettes for sale in Uruguay, were adversely affected by these tobacco control measures.

In 2010, Philip Morris initiated arbitration against Uruguay for breach of its obligations under its bilateral investment treaty (BIT) with Switzerland. In particular, Philip Morris targeted the two legislative measures mentioned above. First, the investor alleged that the Single Presentation Requirement substantially affected the company's value since it had to pull seven of its 13 product variants.[226] Second, it argued that the 80/80 Regulation wrongfully limited Philip Morris' right to use its legally protected trademark by infringing on its intellectual property rights and thus further reduced the value of its investment. Philip Morris argued that the Single Presentation Requirement and the 80/80 Regulation constituted an indirect expropriation of its brand assets, including intellectual property and goodwill associated with each of its brand variants.[227] It further claimed that the measures were arbitrary since they failed to serve a public purpose but caused substantial harm and thus breached the fair and

[226] *Ibid* para 10.
[227] *Ibid* para 180.

equitable treatment standard. Philip Morris sought an order to repeal the Challenged Measures and for compensation of $25 million.

In its defence, Uruguay noted that the measures could not constitute an expropriation mostly because they were a legitimate exercise of its sovereign regulatory power to protect public health.[228] As for the claim on alleged violation of the fair and equitable treatment standard, Uruguay stressed once more that the measures were adopted in good faith and in a non-discriminatory manner and that they were logically connected with the State's public health objectives.[229]

In a majority decision, the tribunal dismissed all the claims made by Philip Morris and upheld the legality of the two tobacco control measures enacted by Uruguay for the purpose of protecting public health. The tribunal ordered Philip Morris to bear all arbitral costs and to pay Uruguay USD 7 million as partial reimbursement of the country's legal expenses. The tribunal by unanimity agreed with Uruguay's argument. Firstly, it confirmed that the measure did not have the effect of substantial deprivation of the investment since Philip Morris was able to continue its business of selling tobacco products in Uruguay. The tribunal could have stopped there, but it was considered relevant to discuss Uruguay's regulatory power to further support its finding that there was no expropriation. In the tribunal's view, Uruguay's adoption of the challenged measures was a valid exercise of the State's police powers.[230] The award makes it very clear that public health policy relates to heightened public welfare concerns. As such, it stated that protecting public health has long been recognized as an essential manifestation of the State's regulatory powers. The tribunal concluded that the Single Presentation Requirement and the 80/80 Regulation have been adopted in fulfilment of Uruguay's national and international legal obligations for the protection of public health. The measures also satisfied the conditions of the regulatory power doctrine as they were adopted in good faith and for the purpose of protecting public health, and they were non-discriminatory and proportionate. Furthermore, the tribunal found the Single Presentation Requirement to be

[228] *Ibid* para 181.
[229] *Ibid* para 310.
[230] *Ibid* para 287.

reasonable because it was an attempt to address real public health concerns.[231] With respect to the 80/80 Regulation, the majority further underlined the importance of deference that has to be given to the State when it has to balance between conflicting considerations and ultimately held that the 80/80 Regulation was a reasonable measure adopted in good faith to implement an obligation assumed by the State under the World Health Organization's (WHO) Framework Convention on Tobacco Control.[232]

1.2.3.2.3 The Azurix Case

The *Azurix Corp. v. The Argentine Republic* case is a clear example that shows the restricted application of the regulatory power doctrine in ISDS tribunals. This case presents an inclusive approach whereby, in order to examine the expropriatory nature of the measures taken by the host State, the ISDS tribunal went beyond the mere impact of the measures on the investment and considered the public purposes behind them.[233] However, despite the legitimate purposes that made the regulatory non-expropriatory, the ISDS tribunal still found them in breach of the fair and equitable treatment standard due to the violation of the investor's legitimate expectation. Thus, the tribunal found Argentina liable to compensate damages incurred by the foreign investor. This is a good example of the point made earlier—namely, that fair and equitable treatment can play a back-up role in favour of investors when indirect expropriation claims fail as a result of regulatory power doctrine.

Azurix Corp v. The Argentine Republic

Azurix Corporation was a U.S. corporation that was participating in the privatization of water services in the Province of Buenos Aires, Argentina. In 1999, Azurix's Argentinean subsidiary, ABA, won the tender for a 30-year concession for the distribution of potable water and the treatment of sewage and paid the fee of 438.5 million Argentine pesos for the Concession. However, from 1999 to 2001, concerns arose about water quality and pressure,

[231] *Ibid* para 410.
[232] *Ibid* para 418.
[233] *Azurix Corp v. The Argentine Republic,* ICSID Case No ARB/01/12, Award 14 July 2006.

after the onset of Azurix's takeover of the Concession. Between 1999 and 2001, provincial authorities allowed political interests to interfere with the tariff regime applied by ABA, hindering the company's ability to increase revenues from water services. The province also failed to fulfil obligations under the Concession agreement related to infrastructure repair works, resulting in an algae outbreak. Later, when an algae outbreak contaminated the water supply, government officials warned citizens not to drink the water, advised citizens to minimize exposure to the water, and dissuaded customers from paying their water bills. Following the incident, Azurix terminated the Concession at the end of 2001, but the province rejected the termination and demanded that ABA continue the provision of the water services. In February 2002, ABA filed for bankruptcy reorganization procedures, and in March 2002 the province terminated the concession agreement, alleging ABA's failure to provide relevant services.

Azurix initiated arbitration proceedings under the Argentina-US BIT, claiming that Argentina's actions, most importantly, constituted expropriation and violated the provision of the fair and equitable treatment standard. Regarding the expropriation issue, Azurix claims that its investment, the Concession Agreement, has been expropriated as a result of "measures tantamount to expropriation." According to Azurix, the province took away Azurix's rights under the tariff regime of the Concession, compromised the ability of ABA to obtain financing, saddled ABA with unexpected expenses by not finishing the promised infrastructure, and took away Azurix's right to recover fully the Canon. The effect of the measures taken not only took away the financial benefits from the Concession by making it unsustainable, but also stripped the investment of its legal security. The investor alleges that these incidents are ground for expropriation. Azurix further claims that Argentina violated the fair and equitable treatment standard, Article II(2)(a) of the BIT, which provides that "[i]nvestment shall at all times be accorded fair and equitable treatment... and shall in no case be accorded treatment less than required by international law." The investor alleges that Argentina breached this standard because Argentina frustrated Azurix's legitimate and reasonable expectations by not allowing to charge tariffs in accordance with the Concession Agreement, by repudiation of Circular, by refusing to accept ABA's termination of the Concession, by refusal to return the non-amortized portion of the investments, by not allowing

ABA to collect the receivables, by requiring that ABA continue to operate the service for more than 90 days, by imposing arbitrary penalties, by politicizing the tariff regime, by publicly calling on customers not to pay their bills, by provoking the illegal intervention of the Provincial Domestic Trade Bureau to enjoin ABA from billing for its services.

In its defence, the host State argues that in order to determine whether or not an expropriation has occurred the government's intention may not be disregarded. Argentina explains that, instead of insisting exclusively on the effect of the measures as the key element, the tribunal must look at the real interests involved and the purpose and effect of the government measure to determine whether an expropriation has occurred. According to the host State, the Province always acted with respect to the Law and the Concession Agreement to protect the public. Argentina noted that all the measures were taken for the protection of public health when problems with water quality arose after an investor took over the provision of water services in Buenos Aires. It needed the tribunal "to consider the elements forming the standard banning expropriation without compensation … [I]t acknowledged the principle of deference to the State in order to define the public interest or usefulness reasons upon which its actions are founded."[234] Regarding the second claim, Argentina questions the facts on which the alleged breach of the fair and equitable treatment standard is claimed by Azurix. The host State denies the contention of Azurix that the fair and equitable treatment standard would refer to the expectations of the investor not being frustrated by legislation, rules and regulations. Instead, the tribunal must examine the impact of the measure on the legitimate and reasonable investment backed expectations of the investor. Referring to the list of expectations raised by the investor, Argentina qualifies them as rash or extremely vague or semantic labels rather than description of the facts. Argentina argues that the basic touchstone of fair and equitable treatment is that a government will obey its own laws and customary international law, will act honestly, transparently, consistently with representations made and in good faith. And since the measures taken by Argentina are within the limits of international law, domestic law, and the contract, Argentina cannot be held responsible for a breach of the BIT, nor can it be held to have breached it even under the standard proposed by Azurix.

[234] *Ibid* para 291.

In 2006, the tribunal rejected Azurix's claim of expropriation as, in its view, the province's actions did not amount to expropriation. In considering Azurix's expropriation claim, the tribunal was called on to decide to what extent the "purpose" underlying government measures was relevant to a determination as to whether such measures constituted expropriation under the US-Argentina treaty. The tribunal notes that the purpose of a regulatory measure is a helpful criterion to determine whether regulatory actions taken by Argentina would be expropriatory and give rise to compensation. In considering each of the grounds which the investor has advanced to justify its expropriation claim, the tribunal will assess them from the perspective of whether Argentina exercises it regulatory power for the public purposes. Given these considerations, the tribunal finds that the actions taken by Argentina are not amounted to expropriation. Having articulated this approach, the tribunal in the Azurix arbitration, would go on to find that the US water-services company had not suffered an expropriation of its contractual rights. However, the tribunal was convinced that Argentina had denied the investors "fair and equitable treatment" as required under the treaty. The tribunal reasoned that what constituted "unfair" and "inequitable" treatment should be determined in light of the legitimate expectations which the investor had when making its investment.

To determine whether the host State breached its obligation to treat the investor's investment fairly and equitably, the tribunal identified various instances where authorities acted unreasonably, engaged in political meddling or politicized discussions related to the tariff regime, thus leading to breach of the "fair and equitable treatment" obligation owed to Azurix. In particular, the tribunal is struck by the conduct of the province after the investor gave notice of termination of the Concession Agreement. ABA had requested to terminate it in agreement with the province. The province refused what was a reasonable request in light of the previous behavior of the province and its agencies. The refusal by the province to accept that notice of termination and its insistence on terminating it by itself on account of abandonment of the Concession is a clear case of a breach of the fair and equitable treatment standard.

1.2.3.2.4 The Copper Mesa Case

Copper Mesa Mining Corporation v. Republic of Ecuador is a case in which the ISDS tribunal found regulatory measures taken by the host State an expropriatory that needs to be

compensated.[235] However, instead of holding the host State liable to fully compensate the foreign investor, the ISDS tribunal referred to Article 39 of the Draft Articles on Responsibility of States for Internationally Wrongful Acts *to reduce the amount of compensation* by 30 per cent. It explained that the investor's injury was caused both by the host State's unlawful expropriation and also by the investor's own contributory negligent acts that reduced the chances of the mining concession held by the investor being a commercial success. In this case, the investor wrongdoing was factored into the tribunal's calculus of the host State's remedies. This approach signals that the host State in investment arbitration proceedings may raise the defence of the investor's contributory fault in order to seek a reduction of remedies. This defence has been later characterized by legal scholars as being an "investment reprisal" approach relied upon in the ISDS tribunal to reduce damages after identifying the host State's breach of its obligation under the expropriation provision in the applicable investment agreement.[236]

Copper Mesa Mining Corporation v. Republic of Ecuador

In 2005, Canadian company Copper Mesa Mining Corporation Exploration (Copper Mesa), through Barbadian and Ecuadorian subsidiaries, acquired the Junín concession in Ecuador. From 2005 onwards, Copper Mesa made a series of expenditures in relation to the concessions. In particular, it commissioned a geological report, acquired a neighboring concession and surface land in and around the concession areas, prepared and submitted an environmental impact study (EIS) for the exploration phase, employed a team of Ecuadorian staff and committed resources to providing social services and community development. In April 2008 Ecuador's Constituent Assembly passed legislation known as the Mining Mandate, which clarifies that "Termination, without economic compensation, is declared for all mining concessions without any investment in project development having been made in their exploration stage by December 31, 2007 or without their [EIS] having been submitted or without a prior referendum process having been conducted, including those pending an

[235] *Copper Mesa Mining Corporation v Republic of Ecuador*, Permanent Court of Arbitration (PCA) No 2012-2, Award 15 March 2016.
[236] See generally Jarrett, *supra* note 191.

administrative resolution."[237] On October 2008, the Under-Secretary of Mines ordered the Regional Director of Pichincha to declare the termination of the Junín concessions "without any compensation whatsoever" on the basis of Article 1 of the Mining Mandate. The reason stated is that EIS consultations had not been carried out by the concessionaire. By the Termination Resolutions, Copper Mesa's Junín concessions were terminated without any economic compensation. For all practical purposes, following the Termination Resolutions, Copper Mesa had lost the Junín concessions.

In 2010, Copper Mesa initiated a claim and contended that the government of Ecuador had violated its obligations under the investment treaty, most importantly its obligations under Article VIII: "Investments or returns of investors of either Contracting Party shall not be nationalized, expropriated or subject to measures having an effect equivalent to nationalization or expropriation (hereinafter referred to as "expropriation") in the territory of the other Contracting Party, except for a public purpose, under due process of law, in a non-discriminatory manner and against prompt, adequate and effective compensation." The investor contended that it is well established that the Termination Resolutions, as order by the Mining Mandate, revoking a concession (or a license) needed to carry on a business activity constitutes an expropriation of the investment. It argued that these measures deprived the investor the entire value of its investments and caused it to suffer substantial damages. The investor further contended that this revocation is an unlawful expropriation under the Treaty as no compensation was paid, it was not taken for a public purpose, it was not carried out according to due process of law, and it singled out the investor's investments in a discriminatory manner. Copper Mesa then claimed that the reparation should take the form of monetary compensation sufficient to wipe out the consequences of the host State's illegal acts.[238]

In its defence, Ecuador rejected these claims and contended that the Mining Mandate is issued by the State in the exercise of its legitimate regulatory powers, responding to compelling public policy considerations, seeking to address the many social, economic, and environmental

[237] *Copper Mesa Mining Corporation v. Republic of Ecuador,* Permanent Court of Arbitration (PCA) No. 2012-2, Award 15 March 2016, *supra* note 235 para 4.3.
[238] *Ibid* para 1.10.

issues that remained unsolved. According to Ecuador, the Mining Mandate was adopted for the purposes of protecting public health and the environment where the requirement to consult the local population on the basis of an EIS was specifically intended to protect the residents and local communities and to reduce the environmental impacts of mining activities. It noted that it is well established under international law that a non-discriminatory regulation, adopted for a public purpose, and enacted in accordance with due process, does not amount to expropriation. In addition, as measures taken pursuant to the Mining Mandate, the Termination Resolutions were also legitimate public policy. It emphasized that "the Termination Resolutions with respect to the Junín concessions were taken following the failure of Ascendant Ecuador to respect and comply with a legal framework in place."[239] Ecuador further explained that when the consultation team intended to carry out the inspection of Junín concessions, as part of the EIS requirements and the Mining Mandate, it was faced with a group of peoples who were ordered by the investor to beat, assault, push, shove, hold guns against the consultation team. Taking all these actions into consideration, Ecuador underlined that the failure to submit an EIS consultations under the Mining Mandate were the cause of the Termination Resolutions. Ecuador contended that Termination Resolutions were not arbitrary and unjustifiable as they were made in compliance with both Ecuadorian law and international law as a result of the concessionaire's failure to submit a valid EIS.[240] Therefore, Ecuador concluded, these measures do not amount to expropriation under the Treaty.

The tribunal decided that the effect of the Termination Resolutions was effectively to neutralize the investor's investment in the Junín concession, amounting to substantial deprivation. It then noted that, "[a]s a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alios, a foreign investor or investment is not deemed expropriatory and compensable."[241] However, the tribunal was concerned with the circumstances and emphasized that given the particular circumstances of the Termination Resolutions, they were "no mere regulatory measures, because, in the circumstances, these Resolutions were made in an arbitrary manner and without due process" and held that "the

[239] *Ibid* para 6.30.
[240] *Ibid* para 4.3.
[241] *Ibid* para 6.6.

permanent taking of the Claimant's Junín concessions was an expropriation" under the Treaty.[242] The tribunal further held that, as regards unlawful expropriation, it was indisputable that the Termination Resolutions were not made or implemented against prompt, adequate and effective compensation as required by Article VIII of the Treaty. Given the absence of any compensation and due process upon such expropriation, the tribunal decides that the permanent taking of the investor's Junín concessions was an unlawful expropriation in breach of Article VII of the Treaty and, thus, was needed to be compensated.

The importance of this decision appears when the tribunal determined damage compensation cost according to "contributory fault."[243] In this award, the tribunal explained that, "[i]n the determination of reparation, account shall be taken of the contribution to the injury by wilful or negligent action or omission of the injured State or any person or entity in relation to whom reparation is sought."[244] It referred to Article 39 of the Draft Articles on Responsibility of States for Internationally Wrongful Acts to explain that the investor's worsening situation as the concessionaire in the Junín area was caused (in whole or in part) by its own fault. The tribunals explained that "by the acts of its agents in Ecuador, the investor had substantially reduced its chances of turning its Junín concessions into a commercial success. In short, a foreign investor, by its local agents, whatever the illegal provocations by local residents in the form of roadblocks, violence, arson and other impediments, should not resort to recruiting and using armed men, firing guns and spraying mace at civilians, not as an accidental or isolated incident but as part of premeditated, disguised and well-funded plans to take the law into its own hands. … It was bound to fail and to make the situation far worse for the Claimant; and it did."[245] It noted that the investor's injury was caused both by the Ecuador's unlawful expropriation and by the investor's own contributory negligent acts and omissions. The

[242] *Ibid* para 6.66.
[243] It should be noted here that "the arbitral tribunal did not explicitly make a finding of investment reprisal, but rather 'contributory fault'. […] The arbitral tribunal's finding is best described as a finding of investment reprisal because this expression most accurately reflects the nature of the investor's conduct which gives rise to the defence," Jarrett, *supra* note 191 at 22. Describing contributory fault as investment reprisal is also mentioned by Salama who notes that "Copper Mesa's misconduct may be conceived of as an affront to state sovereignty that instigated the state to take a measure of reprisal, thus indirectly contributing to its loss," Yasmin Salama, "Obtaining Damages for Corporate Human Rights Violations in Investment Arbitration" (2022) 3:5 Canadian Institute for International Law Expertise Journal of International Law 39–51 at 44.
[244] *Copper Mesa Mining Corporation v. Republic of Ecuador,* Permanent Court of Arbitration (PCA) No. 2012-2, Award 15 March 2016, *supra* note 235 para 6.9.
[245] *Ibid* para 6.99.

tribunal decided that Copper Mesa's negligence to provide appropriate EIS consultations contributed 30 per cent of its loss.

1.3 Holding Foreign Investors Accountable for Breach of International and/or Transnational Environmental Obligations before ISDS Tribunals

The predominantly investor-friendly nature of IIAs and the asymmetrical structure of ISDS tribunals compel legal scholars to grapple with finding a balance between the competing imperatives of safeguarding investments and upholding environmental considerations within investment law. The prevailing view among scholars is to advocate for the revision/re-forming of IIAs to accommodate better States' rights to advance sustainable development. However, this endeavor is anticipated to be prolonged, demanding, and even futile, as I will explore in Chapter 2. As an alternative approach, I will propose a more practical, immediate, and comprehensive solution to hold foreign investors accountable for environmental impacts within ISDS tribunals, given the existing form of IIAs and the existing structure of ISDS tribunals. The approach I will take is one that conceptualizes and operationalizes how international and/or transnational environmental obligations of foreign investors function in ISDS proceedings brought by these investors themselves.

1.3.1 Overview of My Approach

By invoking international and/or transnational rules that impose environmental obligations on foreign investors in the investor-state dispute settlement procedures, I aim to achieve two distinct outcomes. First, this approach will empower host States in proceedings before ISDS tribunals to highlight and address instances where foreign investors fail to adhere to their international and/or transnational environmental obligations. By doing so, host States can justify impacting the economic interests of investors on the basis of the investors' non-compliance with the identifiable environmental obligations. Unlike with the investment reprisal doctrine, under this approach the State can raise violation of obligations as a full defence—such that the state conduct is not a breach of the IIA and, accordingly, such that no compensation is owed by the State to investor. Second, once the host States' defence has been validated, they can pursue a counterclaim against

the foreign investors in ISDS tribunals in order to move from zero compensation to the investor to compensation from the investor to the State. This counterclaim would seek to hold the foreign investors accountable to fully or partially compensate the host States for damages arising from environmentally risky investments and their failure to adhere to international and/or transnational environmental obligations; as with investment reprisals, contributory fault can play a role in determining how much the investor owes the State.

To realize these outcomes, I focus first and foremost on foreign investors' obligations rather than the combined rights and obligations of host States. Instead of relying on arguments that need ISDS tribunals looking beyond the "sole effects" of the measures to examine their impacts on the investment and/or justifying an expanded "regulatory power" of host States to take measures when faced with foreign investors' affront to their environmental rights, I propose the importance of holding foreign investors environmentally accountable before ISDS tribunals. One potential solution for foreign investors' accountability is to invoke the international and/or transnational environmental obligations of foreign investors in ISDS tribunals and resolve investment disputes in light of the international and/or transnational liability law imposing such obligations.[246] On this approach, which is called the "post-establishment illegality defence," host States can assert, in factually conducive situations, that foreign investors lose protection for investments due to the investors' illegal actions after the investment establishment. I will be delaying the detailed discussion of the doctrinal ways in which liability law can be invoked/applied under the plea of the post-establishment illegality defence until Chapter 4. As will be discussed in detail in Chapter 4, the wrongfulness threshold is quite high: investor conduct must involve the failure of foreign investors to comply with identifiable environmental obligations placed on them by international and/or transnational law—and not *mere* breaches of local law or other morally blameworthy conduct.

[246] Xuan Shao, "Environmental and Human Rights Counterclaims in International Investment Arbitration: at the Crossroads of Domestic and International Law" (2021) 24 Journal of International Economic Law 157–179. Briefly, in this dissertation, "liability law" refers to the body of international and transnational legal rules that impose obligations on foreign investors and may be applied by ISDS tribunals as substantive law in the resolution of investment disputes. Such application can result in certain claims being deemed inadmissible or in the reduction of compensation owed by the State to the investor. For a detailed analysis of liability law, see Chapter 2.

As discussed, current investment treaties do not commonly impose substantive obligations on investors other than perhaps requiring foreign investors to establish their investments in accordance with host state law. Illegal conduct of investors at the establishment phase of the investment because of violating national law can result in dismissing the competency of ISDS tribunals to resolve the dispute based on the factual argument that there has been no investment at all that needs to be disputed. Using ISDS tribunals to hold foreign investors accountable is possible only when host States raise concerns about the post-establishment illegality of foreign investors due to their non-compliance with international/transnational obligations during the performance of investments. Therefore, the key question here will be what (if any) international/transnational obligations on the investor are actionable in ISDS tribunals.

For this objective, I analyze the ISDS tribunal's decision in the *Urbaser v. Argentina* case as an illuminating reference point for examining the challenges and opportunities facing host States when they seek to utilize ISDS tribunals as a forum for obliging investors to comply with international obligations (albeit with that forum's availability being dependent on investors having first chosen to bring a claim before it). Unusual and relatively isolated as it currently is in the case law, *Urbaser* will serve as a reference point throughout this dissertation for the approach that can find favour in cases more generally.[247]

In the *Urbaser* case, a body of transnational self-regulated norms[248] imposing obligations on foreign investors, notwithstanding their common characterization as *soft law*—such as the United Nations Global Compact (within the wider category of transnational environmental initiatives)—was invoked by the host State. This body of transnational self-regulated norm was then treated by the ISDS tribunal as substantive law—what I am calling transnationalized customary international law—in the investment dispute settlement procedures.[249] The tribunal's decision

[247] , *supra* note 3.
[248] I shall use "transnational self-regulated norms" and "transnational self-regulatory norms" interchangeably.
[249] Transnationalized customary international law refers to norms emerging from the interactions between States and non-state actors in order to address issues that transcend national boundaries. These norms expand the concept of customary international law to create more consistent global practices and equitable global order by considering non-state actors alongside actors as both object and subject of international law with respect to achieving sustainable development goals (the most relevant global issue area to the subject of my discussion). In Chapter 3, I thoroughly discuss how non-state actors can be involved in the lawmaking process of transnationalized customary international law and also be target of direct international obligations at the transnational level.

in *Urbaser* (discussed below), which relied on allegations of the investor's breach of transnational/international human rights obligations during the post-establishment phase of the investment, is a notable advance in tribunal practice. The case, then, is of paramount importance *as an entry point* for my proposal to hold foreign investors environmentally accountable for their post-establishment illegal conduct because they do not comply with their obligations included in transnationalized customary international law.

1.3.2 The Urbaser Case

The *Urbaser v. Argentina* case is a quite recent investment dispute that can be thought of as a gate opener for holding foreign investors environmentally accountable before ISDS tribunals. This case represents the first and necessary step taken by an ICSID tribunal to recognize the possibility of imposing obligations on foreign investors. In this case, the ISDS tribunal dealt with two intertwined claims: the initial claim brought by the investor and the counterclaim brought by the host States.

Urbaser was a shareholder in a concessionaire that was in charge of the supply of water and sewerage services in the province of Buenos Aires, Argentina. However, emergency measures adopted by Argentina led to financial losses for the concessionaire, resulting in its insolvency. Urbaser initiated arbitral proceedings against Argentina to claim that the host State both violated the fair and equitable treatment standard and expropriated the investment. It then requested damages allegedly caused by Argentina's treatment. The tribunal rejected most of the claims and did not find Urbaser entitled to the requested damages.

For its part, Argentina filed a counterclaim, alleging that the investor's failure to provide the necessary level of investment in the supply services led to violations of the international human rights to water. It sought damages for the breach of international human rights obligations during the performance of the investment. In its decision, the tribunal asserted that human rights law imposes obligations on corporations not to interfere with the right to water. However, the tribunal was not convinced that human rights law requires corporations to take steps to fulfill or protect this right. Thus, it rejected the counterclaim on the grounds that the host State did not provide any

legal grounds for any individual's right to claim damages as a consequence of an alleged violation of the human right to water with respect to positive obligations attaching to that right.

Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic

Aguas Del Gran Buenos Aires, S.A. (AGBA) is a company established by the Spanish corporations Urbaser and Consorcio de Aguas Bilbao Bizkaia (collectively, Urbaser). In early 2000, Argentina granted Urbaser a concession "to expand the drinking water and sewage services" in the Province of Buenos Aires.[250] Over the course of 2001-2002, Argentina was in a financial crisis, prompting a series of financial emergency measures and an adjustment to the tariff regime that caused serious economic losses to Urbaser's concession. Argentina ultimately terminated Urbaser's concession, which resulted in Urbaser initiating an ICSID arbitration pursuant to the Spain-Argentina Bilateral Investment Treaty.[251]

In an *initial claim*, the investor alleged that Argentina breached the provisions of the bilateral investment treaty executed between Argentina and Spain in 1991, in particular, Article IV on fair and equitable treatment and Article V on lawful expropriation. In its claim, Urbaser alleged that, in an effort to attract foreign capital, Argentina had established a Regulatory Framework that was very attractive for investors. The Regulatory Framework contained a set of guarantees designed to provide security to any diligent investor, including the necessary mechanisms to ensure that tariffs were reasonable and that, even faced with monetary crises, tariffs were maintained at adequate levels to cover for service costs and a rate of return, thus preserving the economic and financial equilibrium of the Concession.[252] However, later, by adjusting the tariff regime, Argentina failed to provide such protection and treatment to the investor. The adjustment, it claimed, hindered and even prevented the company's collection of revenue for the services it provided and also caused a significant increase in the

[250] *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, *supra* note 3 para 69.
[251] *Ibid* para 34.
[252] *Ibid* para 561.

Concessionaire's costs. Urbaser alleged that adjusting the tariff regime thereby violated the BIT's fair and equitable treatment standard (Article IV) stating that the fair and equitable treatment standard under which the reasonable expectations of the investor at the time it made the investment–which were based on representations, commitments or specific conditions offered by the State–should be protected. Investors complain that their "justified expectations" with respect to the tariffs to be collected for the services were negatively affected by the actions of the Regulatory Framework. Indeed, the existence of a privatization process and of a commitment to maintain a certain tariff level are generally underscored as conclusive elements in determining the existence of legitimate expectations formed by the investor with regard to the preservation of its rights. The failure to meet such commitments constitutes a breach of the obligation to afford the investment fair and equitable treatment.[253] Therefore, expropriation, and discriminatory and unjustified treatment provisions since they negatively impacted the investment and destroyed "any chance of obtaining the reasonably expected results."[254] Urbaser further argued that the unilateral modification of the Concession Contract by the Argentine Republic and the Government of the Province of Buenos Aires, which caused serious disruption of the economic equilibrium and generated the loss of value of the investments, falls within the concept of indirect expropriation.[255] When there is indirect expropriation, the owner loses the use and the enjoyment of the investment and the benefits deriving from it. Indeed, the Concessionaire's tariffs had been pesified, forcefully converted from U.S. dollar-denominated bank deposit into pesos, reducing their value by two third, any chance to restore the original tariffs had been eliminated and the Regulatory Framework had been substantially modified. The modification of the Regulatory Framework and the refusal to renegotiate the Contract substantially and dramatically reduced the investment's value. This had an effect tantamount to expropriation. According to Article V of the BIT, "nationalization, expropriation or any other measure having similar characteristics and effects," any measure taken by a Contracting State and having effects equivalent to expropriation will generate an inexcusable obligation to compensate on the part of the host State even if no formal expropriation was present.

[253] *Ibid* para 578.
[254] *Ibid* para 562.
[255] *Ibid* para 951.

Argentina, in turn, argued that the Province of Buenos Aires took regulatory measures to protect the public interests and had no alternative but to terminate the concession, given the company's failure to fulfill their obligations under the concession. An addition, the measures taken by Argentina complied with the agreed upon requirements were not discriminatory and were implemented in a well-reasoned manner. In its defence, Argentina noted that the fair and equitable treatment provision does not amount to a guarantee of profitability for foreign investors. It argued that the investor can expect that the host State implements its policies *bona fide* by conduct that is, as far as it affects the investors' investment, reasonably justifiable by public policies. Therefore, the fair and equitable treatment requires good faith, transparent, reasonable treatment, free from arbitrariness and discrimination, and it does not protect any expectations that there will be absolute stability in the legal and commercial framework.[256] Argentina further rejected the claim of expropriation by noting that the measures adopted before the termination did not amount to indirect expropriation because "the emergency measures were necessary to protect essential public interests."[257] Argentine adopted the disputed measures in the legitimate exercise of its police power and of the rights granted by the very Concession contract and the Regulatory Framework. It maintained that the management of its monetary policy is integrally related to the measures adopted to face the crisis and thus Argentina is not liable for economic injury which is a consequence of bona fide regulation. Argentina concluded that the measures taken to guarantee the continuation of the basic water supply to millions of Argentines were not expropriatory in nature and did not produce an effect tantamount to expropriation because the Argentine Republic merely exercised its police power.[258]

The tribunal rejected most of Urbaser's claims. It decided that the fair and equitable treatment standard is not focused exclusively on interests and expectations of a legal nature. It includes the actual social and economic environment of the host State, which is also part of the expectations the investor must acknowledge when making its business decision. The fair and equitable treatment thus does not provide a standard according to which the investor would remain completely isolated and immune from the host State's endeavors to deal with such

[256] *Ibid* para 594.
[257] *Ibid* para 982.
[258] *Ibid* para 988.

situations to advance the public interest. The tribunal explained that the difficulties that the Concessionaire faced were perceptible well before and recognizable in their first serious manifestations already upon the takeover. The serious drop in collectability was one of the consequences of the country's economic degradation, which seriously affected the population living in the province. Another consequence was the difficulty in obtaining financing in amounts as important as to be expected at the takeover. The tribunal confirmed that "these emergency measures are part of the police power held by every State" and went on to hold:

> Their sole purpose was to respond to the most severe crisis in the history of Argentina. The crisis made it necessary to adapt the Regulatory Framework to the newly identified needs. They were aimed at preserving the integrity and legitimacy of the Argentine State. They were regulatory actions aimed at preserving essential services such as the drinking water and sewerage service. They did not affect all or a substantial part of the Claimant's alleged investment, they were not discriminatory, and they were not adopted or applied in bad faith or disregarding Claimants' rights.[259]

To decide about the expropriation claim, the tribunal explained that the basic idea of this claim is that of "taking." In that regard, the effects of these measures taken by Argentina were not unilaterally affecting the income derived from public concession contracts. They were complemented by an undertaking of the authorities to provide for renegotiation of the contracts, which implicitly meant a review of basic contractual parameters that went beyond the adjustment mechanisms anyhow available under the contract. Therefore, the emergency measures were far from any "taking" away of the Concessionaire's rights. They represented a temporary reduction in the Concessionaire's income the effects of which were to be compensated in full or in part through a process of renegotiation to be undertaken and concluded by mutual agreement. Therefore, the Tribunal concludes that the emergency measures taken in 2002 did not represent a "taking" tantamount to an indirect expropriation.[260] The measures did not involve an expropriatory intent or effect simply because they did not entail the expropriation of the investor's investment. Therefore, the expropriation claim submitted by investors should be rejected.

In *a counterclaim*, Argentina requested $USD 404.34 million in damages for Urbaser's failure to provide the necessary investment in the concession. The host State argues indeed that

[259] *Ibid* para 993.
[260] *Ibid* para 1008.

investor' failure to provide the necessary investments caused a violation of the fundamental right for access to water, "which was the very purpose of the investment agreed upon in the Regulatory Framework and the Concession Contract and embodied in the protection scheme of the BIT."[261] By failing to make the investments they had undertaken to make, Argentina argued that the investors violated the principles of good faith and *pacta sunt servanda* in relation to the obligations found in the Universal Declaration of Human Rights of 1948.[262] Argentina argued that the investor's failure to provide the necessary investment caused a violation of the fundamental human right to water.[263]

In its defence, the investor argued against the tribunal's competence to entertain Argentina's counterclaim and noted that the counterclaim is not based on any violation of the Spain-Argentina BIT.[264] The fact that Article X(5) of the BIT designates Argentine law and international law as applicable law does not mean that the BIT requires the investor to comply with such laws or that it elevates their breach to the level of BIT violations that the Argentine Republic could bring before an ICSID tribunal. Because the BIT does not impose obligations upon the investor, it is impossible for the State to rely on a BIT which does not include an umbrella clause to assert a contractual obligation. Urbaser argued: "Respondent's Counterclaim must be dismissed outright, as it is neither within the scope of the Tribunal's jurisdiction nor a dispute arising directly from an investment, as required by Article 25(1) of the ICSID Convention, to which Article 46 thereof and Arbitration Rule 40 implicitly refer."[265] Urbaser further argued that the Universal Declaration of Human Rights "include[s]

[261] *Ibid* para 1151.
[262] Note Argentina's argument does not seem to make a distinction between the non-treaty UDHR and the applicability of the principle that underpins international treaty law, namely, *pacta sunt servanda* (agreements are meant to be kept). Typically, international lawyers do not contend the UDHR, as a General Assembly resolution, is a binding instrument akin to a treaty. Rather, the UDHR as an instrument is referenced as shorthand for the argument that its norms have evolved into customary international law. That said, it is also argued by some that the UDHR is incorporated by reference into the clauses in the UN Charter that reference human rights in general terms; on that line of argument, one might say that the UDHR is subject to the principle of *pacta sunt servanda*—albeit, in formal terms, because the UN Charter as a treaty is.
[263] *Urbaser SA and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic,* ICSID Case No ARB/07/26, Award 8 December 2016, *supra* note 3 para 1156.
[264] The discussion about the ISDS tribunal's competence to entertain Argentina's counterclaim is beyond the scope of this dissertation. By bracketing the tribunal's decision on jurisdiction to hear the counterclaim, I focus on analyzing the merits of the counterclaim.
[265] *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic,* ICSID Case ARB/07/26, Award 8 December 2016, *supra* note 3 para 1128.

specific obligations having to do with drinking water" that are incumbent upon States to guarantee the human right to water, not on private companies like the investor.

Argentina argued that the Declaration avoids referring to who would be responsible for the rights and obligations arising therefrom. However, upon reading the Declaration, it is evident that they do not lie exclusively with States. The Preamble expressly sets forth that the duties would lie both on institutions and on individuals. Article 1 states that its provisions apply to individuals even in private relationships. Article 30 declares that nothing in the Declaration may be interpreted as implying for any State, group or person any right to engage in any activity or to perform any act aimed at the destruction of the rights and freedoms set forth herein. Article 29(1) sets forth that everyone has duties to the community. Therefore, business companies and international corporations are implicated in the obligations included in international human rights law.

Argentina added that the International Labor Organization Tripartite Declaration of Principles concerning Multilateral Enterprises and Social Policy acknowledges that the rules contained in the Universal Declaration of Human Rights are applicable to multinational companies. Argentina thus concluded that "the right to water is an essential human right that represents not only an obligation of States but also, and more importantly, a social right based on a policy to which the whole society has to contribute, based on the understanding of the United Nations." Importantly for the theses of the present dissertation, Argentina went on to link its normative status not just to documents produced under the auspices of international organizations like the UN and the ILO but to transnational instruments generated by companies themselves: "It is a fundamental right that the leading companies of the world have adopted in the Global Compact as being part of their corporate social responsibility."[266] Therefore, it is evident that rules of International Human Rights Law create obligations that must also be respected by multinational companies.

[266] *Ibid* para 1161.

In deciding the merits of the counterclaim, the tribunal first determined that the agreement between the parties that is referred to in Article 42(1) of ICSID Convention is embodied in Article X of the BIT. According to this Article, the applicable rules are the principles and rights contained in the BIT, those contained in other treaties in force between Spain and the Argentine Republic, Argentine law, and the general principles of international law. Therefore, the rules of international law constituted the applicable law in resolving the counterclaim on the basis of Article X in the relevant BIT. The tribunal asserted that the BIT is not a set of treaty rules defined in isolation without consideration given to rules of international law external to its own rules. As the tribunal put it: "The BIT cannot be interpreted and applied in a vacuum…The BIT has to be construed in harmony with other rules of international law of which it forms part, including those relating to human rights."[267] In addition, the tribunal noted that Article VII(1) on "more favourable terms" "states expressly that a source of international law that is external to this BIT can provide more favorable rights that are granted on the basis of Article VII(1) of this BIT and therefore subject to be claimed, if need be, through the dispute resolution mechanism provided in Article X." Thus, the BIT does not represent, in the view of the Contracting Parties and its clear text, a set of rules defined in isolation from consideration given to rules of international law external to its own rules. To fully reflect the terms of Article X, the tribunal must apply the BIT, Argentine law and the general principles of international law applicable to the matter to resolve the counterclaim.

The tribunal also rejected the investors' position that corporations are by nature not able to be subjects of international law and therefore not capable of holding the human right to water in what were asserted to be the exclusive State-to-State relations governed by international law. Instead, it noted that private parties have commitments and indeed legal obligations of compliance in relation to human rights. It explained that the BIT shows that the Contracting States accepted that investors are entitled to invoke rights arising from international law (in addition to the rights resulting from Article X). If the BIT therefore is not based on a corporation's incapacity to hold rights under international law, it cannot be admitted that it would reject by necessity any idea that a foreign investor company could not be subject to international law obligations. The tribunal further observed that international law accepts

[267] *Ibid* para 1200.

corporate social responsibility as a standard of crucial importance for companies operating in the field of international commerce. This standard includes commitments to comply with human rights to water.[268] In light of this more recent development, "it can no longer be admitted that companies operating internationally are immune from becoming subjects of international law."[269] Accordingly, the tribunal decided that basic human rights are complemented by an obligation on multiple actors, both public and private parties, not to engage in activity aimed at destroying such rights.

However, the tribunal noted the human rights to water and sanitation as part of the general notion of human rights are not pertinent in the instant case. After surveying multiple sources, the tribunal found that both investors and States have an obligation to comply with some performances required by public international law. However, the required performances significantly differ. The tribunal confirmed that the human right to water entails an obligation of compliance on the part of the State across the full gamut of obligations that any given human rights generates (to respect/not interfere, to protect from harm by others in society and to fulfil through state provision), but it does not contain obligations beyond the obligation to respect (i.e. not to interfere) on the part of any company providing the contractually required service. Thus, the investor's obligation to ensure the population's access to water is not based directly on international law but on state law that is itself complying with the State's duty to fulfil human rights under international law. This was a reason sufficient to dismiss Argentina's counterclaim.[270]

1.3.3 Commentary on the Urbaser Case

The *Urbaser* case is a significant step toward greater international corporate responsibility and a counterweight to the asymmetry of the ISDS tribunals. In this case, through the proceedings of a counterclaim brought by the host State for damage compensation, the tribunal admitted the host State's post-establishment illegality defence to hold foreign investors responsible for their breach

[268] *Ibid* para 1195.
[269] *Ibid* para 1195.
[270] *Ibid* para 1220.

of the rules of transnationalized international law. That said, the tribunal's decision in *Urbaser* suffers from shortcomings in that the tribunal only vaguely justifies the recourse to the assumed human rights obligations of investors within traditional international law. In this dissertation, I seek to go beyond its shortcomings in order to examine the central inquiry of my dissertation: how may foreign investors be held environmentally responsible in ISDS tribunals as a consequence of such obligations as these investors may have in transnationalized international law?

1.3.3.1 Significance

The award is significant for three reasons:

1 It concludes that transnational corporations are subjects of international law and can be directly obliged by the rules of international law.[271]

2 It provides the most to-the-point instance yet of an ISDS tribunal effectively involving rules of international law that are external to the specific BIT as substantive law in the investment dispute settlement procedures.[272]

3 It resolves the dispute in accordance with transnational environmental initiatives such as the United Nations Global Compact (UNGC) that is not included in traditional sources of international law.

In the *Urbaser* case, the tribunal took the view that the investment treaty imposes obligations on the host State rather than the investor. It states that "the BIT does not impose obligations upon the investor … [and] does not create obligations for the investor or subject the investor to the rules of

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[271] "Direct" means international law directly impose obligations on investors as opposed to a situation in which investors are environmentally obliged under national law, including where national law is enacted in order to meet States' international duties to regulate private sector conduct—where there is not or may not be a corresponding direct international obligation on the investor. In international law, we also sometime speak of "indirect responsibility" of the State 'for' private conduct—which stems from the existence of positive duties on the State to prevent or act in response to private harmful conduct where the conduct of the private actor need not itself be (directly) unlawful under international law.

[272] In this case, although the investor argued that any claim brought before the tribunal must be on the basis of an alleged violation of the BIT and thus the counterclaim on the basis of an alleged violation of international human rights is outside the tribunal's competence, the tribunal's finding is different. By accepting international obligations of corporation as substantive law, the tribunal rejected the investor's argument. The competence of the tribunal is tied to the question of whether the breach that generated a dispute relating to an investment, and not to the source of the international obligation.

Argentine or international law either."[273] However, it disagreed with the investor's argument that there were no international obligations at all on the investor, noting that guaranteeing the human right to water is not a duty borne solely by the State but may be borne also by private companies like the investor. The tribunal further reasoned that, since "the BIT therefore is not based on a corporation's incapacity of holding rights under international law, it cannot be admitted that it would reject by necessity any idea that a foreign investor company could not be subject to international law obligations."[274] The tribunal reinforced this observation by observing that, as a matter of general law, "it can no longer be admitted that companies operating internationally are immune from becoming subjects of international law."[275]

The tribunal then continued by observing that rules of international law that are external to the BIT, including corporations' commitments to comply with human rights, could be used in the dispute settlement procedure. On this point, the tribunal referred to the provision on the law applicable to the tribunal's decision contained in Article X(5) of the treaty, the tribunal shall apply "the law of the host State and such rules of international law as may be applicable." This statement nullifies the position that the BIT is to be construed as an isolated set of rules of international law for the sole purpose of protecting investments through rights exclusively granted to investors. Such a view is justifiable with respect to Article X(1) that states the possible scope of claims to be submitted to arbitration is not limited to rights directly based on the application (or interpretation) of the BIT: "disputes arising between a Party and an investor of the other Party in connection with investments within the meaning of this Agreement." Considering the BIT as a closed system strictly preserving investors' rights under the BIT would not fully reflect the terms of Article X(1) and would deprive this provision of part of its meaning.[276] Article 42(1) of the ICSID Convention also confirms this understanding.[277] Pursuant to this provision, in the absence of an agreement on the choice of applicable rules of law, the tribunal shall apply the law of the host State "and such rules of international law as may be applicable." Therefore, Article X(5) is in harmony with Article 42(1) of the ICSID Convention, stating that,

[273] *Urbaser SA and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic*, ICSID Case No ARB/07/26, Award 8 December 2016, para 1169.
[274] *Ibid* para 1194.
[275] *Ibid* para 1195.
[276] *Ibid* para 1191.
[277] In Chapter 2, I comprehensively discuss Article 42(1) of the ICSID Convention in detail.

the ICSID Convention does not provide for any restriction in respect of these "applicable rules of international law," which are not circumscribed by the applicable BIT only.[278] In addition, Article VII(l) on "more favorable terms"— "Where a matter is governed by this Agreement and also by another international agreement to which both Parties are a party or by general international law, the Parties and their investors shall be subject to whichever terms are more favorable" —states expressly that a source of international law that is external to this BIT can provide more favorable "terms" without limiting the notion of terms to only "rights" of investors—versus also their "obligations." Therefore "it can thus be retained that the BIT does not represent, in the view of the Contracting Parties and its clear text, a set of rules defined in isolation without consideration given to rules of international law external to its own rules."[279] To further ground its decision to involve external rules of international law, the tribunal referred to Article 31(3)(c) of the Vienna Convention on the Law of Treaties that indicates treaty interpretation should be conducted in accordance with "any relevant rules of international law applicable in the relations between the parties." This rule means the investment treaty cannot be interpreted and applied in a vacuum, instead it should be placed in the overall system of international law.[280] The tribunal then concluded that "the Tribunal must certainly be mindful of the BIT's special purpose as a treaty promoting foreign investments, but it cannot do so without taking the relevant rules of international law into account. The investment treaty has to be construed in harmony with other international law rules, including those relating to human rights and are also applicable to the parties to the dispute.[281]

The tribunal finally drew on a series of international legal instruments to contextualize "a corporation's specific activities as they relate to the human right at issue."[282] Most importantly, the tribunal referred to the Universal Declaration on Human Rights (UNDHR) and the International Labor Organization (ILO) Tripartite Declaration of Principles concerning Multilateral Enterprises and Social Policy to source the international human rights obligations of the investor. These sources, as instruments, are typically categorized as non-binding soft-law

[278] *Ioan Micula, Viorel Micula, SC European Food SA, SC Starmill SRL and SC Multipack SRL v Romania [I]*, ICSID Case No ARB/05/20, Award 11 December 2013, para 373.
[279] *Ibid* para 1192.
[280] *Ibid* para 1201.
[281] *Ibid* para 1200.
[282] *Ibid* para 1195.

norms as they are not treaties and also are recommendatory within the institutional system within which they were adopted.

Article 25 of the 1948 Universal Declaration of Human Rights expresses: Everyone has the right to a standard of living adequate for the health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond his control. The use of the word "including" indicates that this catalog of rights was not intended to be exhaustive. The right to water clearly falls within the category of guarantees essential for securing an adequate standard of living, particularly since it is one of the most fundamental conditions for survival. The proclamation paragraph of the Declaration, which immediately precedes the itemization of the rights, arguably makes this even clearer: "The General Assembly, …Proclaims this Universal Declaration of Human Rights as a common standard of achievement for all peoples and all nations, to the end that *every individual and every organ of society*, keeping this Declaration constantly in mind, shall strive by teaching and education *to promote respect* for these rights and freedoms *and by progressive measures, national and international, to secure their universal and effective recognition and observance*, both among the peoples of Member States themselves and among the peoples of territories under their jurisdiction".[283] Article 1 implies that the UDHR's provisions apply to individuals even in private relationships: All human beings are born free and equal in dignity and rights. They are endowed with reason and conscience and *should act towards one another in a spirit of brotherhood.*"[284] Article 30 declares: "Nothing in this Declaration may be interpreted as implying for any State, *set forth herein*."[285] Article 29 provides: "*Everyone has duties to the community* in which alone the free and full development of his personality is possible."[286]

[283] United Nations, *Universal Declaration of Human Rights (UDHR)* (1948), online: <https://www.un.org/sites/un2.un.org/files/2021/03/udhr.pdf> (emphasis added).
[284] United Nations, *Universal Declaration of Human Rights (UDHR)* (1948), online: <https://www.un.org/sites/un2.un.org/files/2021/03/udhr.pdf> Article 1 (emphasis added).
[285] United Nations, *Universal Declaration of Human Rights (UDHR)* (1948), online: <https://www.un.org/sites/un2.un.org/files/2021/03/udhr.pdf> Article 30 (my emphasis added).
[286] United Nations, *Universal Declaration of Human Rights (UDHR)* (1948), online: <https://www.un.org/sites/un2.un.org/files/2021/03/udhr.pdf> Article 29 (my emphasis added).

Principle 8 of the International Labor Organization Tripartite Declaration of Principles concerning Multilateral Enterprises and Social Policy further states "all the parties concerned by this Declaration should … respect the Universal Declaration of Human Rights and the corresponding International Covenants adopted by the General Assembly of the United Nations as well as the Constitution of the International Labour Organization and its principles according to which freedom of expression and association are essential to sustained progress." In parts of the award, the tribunal referred to corporate social responsibility as a reference point for international obligations of the investor. It mentioned that "international law accepts corporate social responsibility as a standard of crucial importance for companies operating in the field of international commerce."[287] By bringing corporate social responsibility into the picture to support the subjectivity of corporations, the *Urbaser* tribunal acknowledged that instruments generated by corporations themselves, such as the Global Compact, can contextualize a corporation's obligations as they relate to human rights.[288] It is therefore to be admitted by tribunals that "the human right for everyone's dignity and its right for adequate housing and living conditions are complemented by an obligation on all parts, public and private parties, not to engage in activity aimed at destroying such rights."[289]

1.3.3.2 Shortcomings

Major shortcomings of the *Urbaser* award appear when the tribunal vaguely contextualizes the human rights obligations of investors within traditional international law. Indeed, the tribunal did not provide adequate elaboration with respect to how and why these rules of international law are *relevant* and *applicable* to the substance of this investment dispute. The tribunal, without any explanation, applied a series of (presumptively or seemingly) non-binding norms of international law (soft law) to hold foreign investors internationally responsible (subject to the above-described paring back of corporate obligations to those of non-interference only). As such, *Urbaser* takes a serious step toward imposing international legal obligations on foreign investors. However, the tribunal fails to provide in-depth doctrinal analysis and theoretical argument on why and how these norms could be invoked and applied in dispute settlement procedures. It also

[287] *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, *supra* note 3 para 1195.
[288] *Ibid* para 1161.
[289] *Ibid* para 1199.

is very cavalier in the ease with which it concludes that human rights operate only as negative rights when it comes to corporate obligations and leaves positive obligation to States.[290] The tribunal decided that the investor's positive obligation to perform had as its source domestic law alone because general international law goes no further—in this tribunal's undeveloped view—than directly imposing a negative obligation to abstain on corporations (i.e. a prohibition on corporate actors taking actions—versus engaging in omissions—that violate human rights); the underlying theory—undeveloped in the tribunal's reasons—is that positive obligations in the form of ensuring human-rights-required services lie exclusively with the state.[291]

Despite the novelties of this decision and its potential importance, the tribunal's decision is not entirely robust and avoids clear answers to critical questions. The tribunal did not provide much by way of explaining:

1) why exactly any given international law rule beyond the relevant IIAs is relevant as substantive law to resolve investment disputes? (primarily a matter of doctrinal reasoning within established legal understandings); and
2) how soft norms can generate not just legal obligations at the international level but obligations on corporate actors? (primarily a matter of foundational theoretical justification).

Regarding the first question, what should ideally have been discussed is the domain of substantive law in resolving investment disputes. ISDS tribunals consider IIAs to be the fundamental reference point for resolving investment disputes.[292] However, this does not mean that ISDS tribunals apply *only* IIAs to the substantive aspects of investment disputes; instead,

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[290] However, the tribunal's reasoning that corporations like States cannot have positive duties is challenged by recent legal scholars such as Tamara Horbachevska, Josephine Van Zeben & Nadia Bernaz, "A capability approach to the sustainable development goals: towards positive corporate human rights obligations" (2024) 15:3 Transnational Legal Theory 465–492. In this article, the authors argue that the SDGs should be viewed through the lens of the capability approach that normatively instils the SDGs with positive human rights protection obligations not only for States but also for business actors, obliging business actors to not merely refrain from breaching human rights but to actively afford affected individuals and communities with capabilities that ensure the protection and fulfilment of their human rights where the business actors are in a sufficiently compelling relationship to be placed under such duties.

[291] *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, *supra* note 3 para 1210.

[292] Rudolf Dolzer & Christoph Schreuer, *Principles of International Investment Law* (Oxford University Press, 2012).

they do often enough invoke other legal sources to interpret investment treaties. As will be discussed in some detail in the coming chapters, external legal sources can be engaged in the treaty interpretation process if they meet certain requirements. Despite this solid doctrinal backdrop, the *Urbaser* tribunal is silent as to the legal reasoning by which the selected international declarations were to be sufficiently relevant as to be substantive law alongside the IIA's own text.

Regarding the second question, as a matter of international law, a common (and, likely, still dominant) understanding is that norms enshrined in the Universal Declaration of Human Rights and the International Labor Organization Tripartite Declaration of Principles concerning Multilateral Enterprises and Social Policy remain non-binding even for States and that any international legal bindingness needs to be traced to either customary law or treaty text (like the UN Charter and ILO Statute) and not to these two instruments themselves. Furthermore, they are traditionally seen as doubly soft when it comes to corporations, applying only indirectly to them (versus to States) and being voluntary in the sense that companies are free to choose if they wish to comply with the moral expectations expressed therein. The tribunal has not explained how these rules could establish an international obligation of investors, given their generally understood lack of status as binding sources of international law. In addition, the tribunal falls short of theoretically analyzing the international legal subjectivity of foreign investors and does not indicate how foreign investors could be subject to these non-binding norms at the international level.[293]

Notwithstanding the limitations of *Urbaser*, I build on the novelties of this award and benefit from the questions directed against this decision in order to examine the central inquiry of how foreign investors could be held environmentally responsible in ISDS tribunals. Therefore, the next stage in introducing environmental obligations of foreign investors into ISDS tribunals will be to determine, with more precision, which rules of international law are relevant and applicable

[293] There are meaningful differences between the Universal Declaration of Human Rights and the International Labor Organization Tripartite Declaration of Principles concerning Multilateral Enterprises and Social Policy, which may make one or the other more susceptible than the other to the argument that the instrument is hard law—or has evolved into hard law of another form—not soft law and/or that the instrument (or its hard-law analogue) places obligations on corporate actors and not simply on States. However, the tribunal does not come close to addressing such specificities because it does not even grapple with the more general preceding challenges.

to the substances of investment disputes and then are capable of forming the basis of host States' post-establishment illegality defence. For this objective, I will first conduct a doctrinal analysis and second theoretical study to explain that transnationalized customary international law imposing environmental obligations on foreign investors are both relevant to the subject matter of investment disputes and are applicable to the foreign investors in order to mitigate the privileged position of foreign investors as mere rightsholders under international law. As a result, foreign investors can be held environmentally responsible before investment tribunals, even if this only occurs through States invoking corporate obligations as a defensive shield to a claim against a State initiated by a corporation. What *Urbaser* decided and what *Urbaser* did not do by way of reasoning sets the scene for the next three chapters of my dissertation in which I will a) discuss substantive law in investor-State dispute settlement tribunals, b) theorize the legal status of transnational self-regulated norms (soft law) as transnationalized international customary law, and c) study the potential of the UNGC, a prominent example of transnational environmental initiatives, to be used as liability law to be read into international investment law's existing post-establishment illegality defence, in order to hold foreign investors environmentally responsible before ISDS tribunals. For the purpose of the third object, I will reintroduce the *Urbaser* case, in Chapter 4, but this time offering a more detailed analysis of the legal arguments—both explicit and implicit—raised by the host State and accepted by the tribunal under the post-establishment illegality defence.

Chapter 2: Substantive Law in Investor-State Dispute Settlement Tribunal

2.1 Introduction

To align foreign direct investments (FDIs) with *the 2030 Agenda*'s sustainable development goals (SDGs), legal scholars often propose two potential strategies aiming at reforming international investment agreements (IIAs) to become sustainable development-oriented schemes. First, IIAs must reserve sufficient policy space for governments to facilitate investments in sectors conducive to sustainable development.[294] Second, IIAs must include sustainability-relevant provisions to incentivize certain investments that are desirable from the environmental perspective.[295] These strategies would ensure that IIAs promote not just any kind of foreign investment but sustainable ones in order to balance the competing priorities of investment protection and environmental consideration in investor-state dispute settlement (ISDS) tribunals.

Given the criticisms over the one-sidedness of ISDS tribunals and investment agreements discussed in Chapter 1, putting these potential strategies into practice relies mainly on reforming the way that IIAs are currently designed to include sustainable development provisions.[296] Confirming this, the proportion of concluded IIAs that contain environmental language began to increase from about 2002 onwards, reaching a peak when 89% of newly negotiated treaties contained references to environmental concerns.[297] This language can be witnessed in the 2012 U.S. Model Bilateral Investment Treaty[298] and the 2019 Netherlands Model Investment Agreement,[299] which include many provisions explicitly referring to sustainable development

[294] Van Harten, *supra* note 151.
[295] Marie-Claire Cordonier Segger, Markus Gehring & Andrew Wardell, "REDD+ Instruments, International Investment Rules and Sustainable landscapes" in Christina Voigt, ed, *Research Handbook on REDD-Plus and International Law* (United Kingdom: Edward Elgar Publication, 2016).
[296] Gordon, *supra* note 16.
[297] Gordon & Pohl, *supra* note 185.
[298] *A Treaty Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and the Reciprocal Protection of Investment* (2012), online: <https://ustr.gov/sites/default/files/BIT%20text%20for%20ACIEP%20Meeting.pdf>.
[299] *Agreement on Reciprocal Promotion and Protection of Investments between ... and the Kingdom of the Netherlands* (2019), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5832/download>.

issues. Prominent international organizations have also formulated model IIAs addressing sustainable development needs. For example, in 2006, the International Institute for Sustainable Development (IISD) put forward a Model International Investment Agreement for the Promotion of Sustainable Development as a template for IIA-making.[300] The United Nations Conference on Trade and Development (UNCTAD) also updated the Investment Policy Framework for Sustainable Development in 2015 to reflect new generations of sustainable development investment policies.[301] Such an approach is further reflected in the recent Free Trade Agreement between the United States, Mexico, and Canada, where sections are devoted to protecting the environment and promoting corporate social responsibility.[302]

These policy frameworks offer strategic guidance and concrete suggestions for making IIAs more compatible with sustainable development objectives at international and national levels.[303] For instance, the 2016 Morocco-Nigeria BIT contains these techniques: requiring that investments contribute to the sustainable development of the host country (to be covered by the definition of investment in the treaty), requiring that joint commissions be established with representatives of state parties, and requiring provisions on the obligations of investors concerning both environmental and social development.[304] Likewise, the 2009 Canada-Jordan BIT contains a procedural provision for the consultation of experts on environmental law in arbitral tribunals.[305] According to this clause, the disputing parties may appoint one or more experts to report to it in writing on any factual issue concerning environmental, health, safety, or other scientific matters.

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[300] *IISD Model International Agreement on Investment for Sustainable Development*, by Howard Mann et al (International Institute for Sustainable Development (IISD), 2006) online: <https://academic.oup.com/icsidreview/article-lookup/doi/10.1093/icsidreview/20.1.91>.
[301] United Nations Conference on Trade and Development (UNCTAD), *Investment Policy Framework for Sustainable Development* (2015), online: <https://unctad.org/publication/investment-policy-framework-sustainable-development-2015-edition>.
[302] Office of the United States Trade Representative, *Benefits for the Environment in the United States-Mexico-Canada Agreement*, online: <https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/benefits-environment-united-states-mexico-canada-agreement>.
[303] For an in-depth discussion on how investment agreements can be used to promote more sustainable development see Cordonier Segger, *supra* note 7.
[304] *Reciprocal Investment Promotion and Protection Agreement between the Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria* (2016), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaties/tips/3711/morocco---nigeria-bit-2016->.
[305] *Agreement between Canada and the Hashemite Kingdom of Jordan for the Promotion and Protection of Investments* (2009), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bit/787/canada---jordan-bit-2009->.

These treaty examples would enhance the supply of environmental-considerations norms, preserve the State's regulatory power, and enable IIAs to move more generally in the direction of granting more flexibility to host States in regulating critical aspects of their economic system in the interest of the society at large.

However, reforming the existing IIAs in order to promote and protect sustainable investments in ISDS tribunals faces substantial challenges. In addition to legal and technical complexity of reforming existing treaties that may jeopardize the coherency of IIAs, the current investment governance regime was developed at the hands of capital-exporting countries. The constructed subject matter (area) of *investment law* plays a significant role in interpreting IIAs and intends primarily to protect foreign investments from the discriminatory conduct of host States. Thus, reforms aimed at sustainability may result in conflict of interests among existing investment protection goals of IIAs, often prioritizing financial returns over environmental, social, or governance objectives, and newly added sustainable development provisions. Investors and multinational corporations also perceive such reforms as potentially discouraging investment and resist changes that limit their rights or impose additional obligations on them. Lawyers and arbitrators within the ISDS system likewise may resist reforms that could reduce the predictability or profitability of arbitration.[306] The parallel acceptance of the fragmentation of international law further makes it more difficult for IIAs to be more responsive to sustainable development needs because such acceptance serves as a basis for an interpretive community centered on a single treaty or a single field of similar treaties to pursue what is viewed as the separate normative logic of that treaty or field.[307] The global landscape of IIAs includes

[306] Pia Eberhardt & Olivet Cecilia, *Profiting from Injustice: How Law Firms, Arbitrators and Financiers Are Fuelling an Investment Arbitration Boom* (Brussels: Corporate Europe Observatory: Transnational Institute, 2012); Martins Paparinskis, "The Limits of Depoliticisation in Contemporary Investor-State Arbitration" (2012) 3 Select Proceedings of the European Society of International Law 271–285.

[307] The construction of "investment law" emerges from the informal activity of lawyers, arbitrators, diplomats, pressure groups, through shifts in legal culture and in response to practical needs of specialization that mirrors the functional diversification of the international society seeking to articulate or strengthen preferences and orientations that seem not to have received sufficient attention under the general law. The application of special principles of "investment law" by specialized implementation organs of ISDS tribunals is a visible feature of this (self)-constructed legal community. The foregoing observation draws on various approaches to field-specific normative "logics" that are found in work as methodologically and theoretically diverse as Ian Johnstone, Michael L Barnett & Raymond Duvall, "The Power of Interpretive Communities" in *Power in Global Governance* (Cambridge, UK: Cambridge University Press, 2004) 185; Ian Johnstone, "Treaty Interpretation: The Authority of Interpretive Communities" (1991) 12:2 Michigan Journal of International Law 371; Andrea Fischer-Lescano & Gunther Teubner, "Regime-Collisions: The Vain Search for Legal Unity in the Fragmentation of Global Law" (2004) 25 Michigan

thousands of treaties with varying investment protection provisions that makes harmonized reforms challenging.[308] Thus, it has long been argued by investment arbitrators that they have jurisdictional competence only in resolving investment protection issues—an argument aided, implicitly or explicitly, by assumptions that arbitrators' professional expertise and thus institutional competence is in investment law not other fields. Therefore, sustainable development subjects should be addressed through other tribunals and courts resolving disputes related to international environmental treaties or international human rights treaties.

Moreover, notwithstanding the evolving backdrop of the negotiation of new IIAs that include environmental clauses, most investment disputes are still based on IIAs signed in the 1990s or earlier. Evolution itself points to a judicial restraint as an additional reason for arbitrators to take the view that they work with legacy treaty texts that are not for them to interpret in an activist fashion; rather, they must await States' decisions to change the text. According to the United Nations Conference on Trade and Development (UNCTAD), "[i]n 2019, arbitral tribunals rendered at least 71 substantive decisions in investor-state dispute settlement (ISDS) cases…Most decisions concerned were cases based on old-generation international investment agreements (IIAs) signed in the 1990s or earlier."[309] Likewise, "in 2020, at least 68 known treaty-based investor-state dispute settlement (ISDS) cases were initiated. Most investment arbitrations were brought under international investment agreements (IIAs) signed in the 1990s or earlier."[310] This shows that, although vital initiatives are aimed at reforming IIAs to become sustainability-oriented, emerging investment disputes are not primarily settled under IIAs with environmental clauses. In addition, even under some new IIAs, one might question whether including broad references to environmental considerations is sufficiently helpful in guiding arbitrators in their assessment of concrete disputes given their lack of expertise in such a field, given the above-discussed dimensions related to legal culture and interpretive community, given the resulting

Journal of International Law 999; Yves Dezalay & Bryant G Garth, *Dealing in Virtue: International Commercial Arbitration and the Construction of a Transnational Legal Order* (Chicago: University of Chicago, 199 AD).

[308] See Stephan W Schill, *The Multilateralization of International Investment Law* (Oxford University Press) for the discussion on the fragmented nature of international investment law due to the large number of bilateral and regional treaties, emphasizing the complexity of aligning their provisions

[309] United Nations Conference on Trade and Development (UNCTAD), *Review of ISDS Decisions in 2019: Selected IIA Reforms Issues* (2021) at 1.

[310] United Nations Conference on Trade and Development (UNCTAD), *Investor–State Dispute Settlement Cases: Facts and Figures 2020* (2021) at 1.

tendencies to work within frames of reference that embrace fragmentation as a normative fact and investment law as essentially a "self-contained regime" resistant to importing norms from other subject area fields, and given the accretion of decisions over decades that are imbued with such frames of reference.

These challenges suggest that reforming IIAs will not necessarily push ISDS tribunals to consider environmental values in a meaningful way in their decision-making process. Therefore, there is a real need for a more practical approach to deal consistently with investment protection disputes involving environmental concerns. In order to harness the potential for all IIAs to promote sustainable development, we must understand how and why ISDS tribunals have generated a unitary sub-system of principles biased in favor of foreign investors with little formal room for safeguarding the environment of host States (or rather, with little formal room as understood by many, or even most arbitrators).[311] As such, instead of considering the texts of IIAs themselves as the main barrier to sustainable development, I will direct my analysis toward revealing the more fundamental obstacles. These obstacles are embedded in the structural features and legal culture of ISDS institutional mechanisms that all but confine the domain of substantive law to IIAs that primarily (and actively) protect foreign investments.[312] In this regard, I intend to examine whether, if transnational self-regulatory norms concerning environmental obligations of foreign investors were recognized as substantive law—transnationalized customary international law—and more consistently incorporated into the investment dispute settlement process, ISDS tribunals could make progress towards the *2030 Agenda*'s SDGs. Transnationalized customary international law refers to a set of self-regulated norms emerging from the interactions between States and non-state actors in order to address issues that transcend national boundaries. These norms expand the concept of customary international law to create more consistent global practices and equitable global order by considering non-state actors alongside state actors as both object and subject of international law in achieving sustainable development goals, the most relevant global issue to the subject of my discussion.[313]

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[311] For another discursive dimension of what shapes the investment-law arbitral community at a very deep level, see Islam, *supra* note 60.
[312] Mann & Von Moltke, *supra* note 182 at 20.
[313] In Chapter 3, I thoroughly discuss how non-state actors could be involved in the lawmaking process of transnationalized customary international law and also be target of direct international obligations at the transnational level.

This idea was ignited by the tribunal's decision in *Urbaser*, which considered allegations of the investor's breach of international and/or international human rights obligations.[314] The tribunal notably treated transnational self-regulatory norms—such as the United Nations Global Compact—that not only lie outside the specific investment agreement but also are not part of the traditionally understood sources of international law available for selection as substantive law governing the dispute. Taken together, this case provides a valuable foundation for advancing the argument that foreign investors can be held accountable for environmentally harmful conduct where such conduct involves non-compliance with obligations rooted in transnationalized customary international law.

It is worth noting here that in international law there is no sharp distinction between substantive law and procedural law: legal scholars explain "the rules which govern the procedure for settling international disputes are generated and take effect in an 'indistinguishable' manner to the substantive rules which are applied to resolve the subject-matter of the dispute."[315] To establish a working distinction between the two concepts, "international courts and tribunals have sometimes articulated the distinction as being between, on one hand, the rules governing the relations of the parties while conducting a contentious dispute with the court or tribunal hearing it (which are 'procedural') and, on the other hand, the rules governing the relations between the parties more generally (which are 'substantive')."[316] Despite the importance of both species of law in the investment dispute settlement process, in my dissertation, I am not discussing the procedural side of ISDS tribunals in the sense of narrow procedural doctrine. Instead, I focus on rules resolving the substantive issues raised before ISDS tribunals.

In the investment dispute settlement process, substantive law is obviously determinative of outcomes as it governs the substance of the disputes and administers the conduct of parties to the dispute in any given circumstances. By focusing on the outcome-determinative nature of

[314] See Chapter, *supra*, 1 for the discussion of the *Urbaser* case, at pp 92-108.
[315] Chester Brown & Rhys Carvosso, "The Interplay between Substantive and Procedural Law in the Settlement of International Disputes" in Joanna Gomula, Stephan Wittich & Markus Stemeseder, eds, *Research Handbook on International Procedural Law* (Edward Elgar Publication, 2024) 599 at 599.
[316] *Ibid* at 601.

substantive law, which determination cannot ignore that frames of reference of an enclosed interpretive community drives the reading of such law, I will propose a practical approach whereby foreign investors could be found environmentally accountable before ISDS tribunals through arbitrators treating transnational self-regulated norms as imposing environmental obligations on investors and treating that law as substantive law in resolving investment disputes.[317] To be clear, this new approach does not assume substantive analysis alone can be transformative. Consistent with the focus on human hands at the helm of institutional mechanisms, it is understood that, ultimately, substantive argument needs to persuade flesh-and-blood investment arbitrators sufficiently to be acted on and apply external rules of international law (i.e., here, transnational self-regulated norms which are "external" to the text of IIAs) to the content of investment disputes—such that persuasion will have to occur in the face of the resistance inculcated by the construction of that arbitral community's received understandings. Bracketing the issues of whether the ISDS system ought to be changed structurally and how IIAs texts should be reformed substantively, I aim to show that, within the current structure of ISDS tribunals and existing texts and formats of IIAs, finding pathways for transnational self-regulated norms to be considered as part of the substantive law governing the merits of investment disputes would improve arbitral decision-making standpoint by opening doors to integrating meaningful environmental considerations as a matter of binding (liability) law (versus, for example, more nebulous background moral values).[318]

Accordingly, the primary line of argument for this chapter is to explain interpretive approaches used by ISDS tribunals when determining substantive law and to describe to what extent, and in what circumstances, and how ISDS tribunals sometimes do interpret IIAs with respect to customary international law. In other words, what I am principally concerned with, here, is the reasoning and legal language used by ISDS tribunals to either justify or reject the incorporation

[317] Note that, when I say "accountable," I do not mean solely or even mostly in the procedural sense of investors being subject to claims initiated by States. I mean, rather, all three of the following: that any international environmental obligations applicable to them can be invoked as part of the legal analysis as to whether (a) a State can defend itself from bearing responsibility or liability for damages—or as to the extent of such responsibility or liability; (b) whether a State can seek accountability via a counter-claim once the investor opens the door by initiating a claim against the State under an IIA; and c) whether the treaty allows States to initiate their own claims based on either obligations placed on the investor by the treaty or by parallel international law.

[318] In Chapter 4, I explain the role of liability law in holding foreign investors accountable for environmental considerations at the international level.

of customary international law imposing environmental obligations on foreign investors into their interpretation of IIAs.[319] The more expansive application of custom as free-standing law—where permitted by the IIA's jurisdictional remit and/or the scope of Article 41(1) of the ICSID treaty discussed below—will appear as a secondary line of argument in this chapter and subsequent chapters at appropriate points in the discussion.

For this objective, I first review the literature on Article 42(1) of the ICSID Convention on substantive applicable law in investment disputes.[320] This is then followed by case law analyses on leading decisions of ISDS tribunals to know the roles of each of IIA, domestic law, and international in resolving investment disputes. Second, I provide an overview of Vienna Convention on the Law of Treaty (VCLT) methods to manage interaction among different regimes of international law, including, notably, where one or more of those regimes are understood as "self-contained" regimes.[321] Understanding the VCLT to serve as a mandatory reference point for treaty interpretation is of paramount importance to know if customary international law imposing environmental obligations on foreign investors could be used in the investment dispute settlement procedure. Third, I study authoritative decisions of international

[319] Since in Chapter 3, I will discuss the potential of transnational self-regulated norms to be considered as transnationalized customary international law and then be applied in ISDS tribunals, the scope of this chapter is consciously narrow to deal with the interpretation of investment treaties only by reference to customary international law.

[320] Article 42(1) of the ICSID Convention outlines the applicable law that arbitral tribunals must use when resolving disputes under the Convention. Here is the text of Article 42(1):

> The Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable.

[321] Article 31 of VCLTT is a fundamental provision that guides the interpretation of treaties. It outlines the general rule of treaty interpretation and provides guidance on the factors to be considered in determining the meaning and scope of treaty provisions. Article 31 reads:

> 1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.
> 2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:
> (a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
> (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.
> 3. There shall be taken into account, together with the context:
> (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
> (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
> (c) any relevant rules of international law applicable in the relations between the parties.

tribunals/courts on substantive law, the rules of treaty interpretation, and techniques of legal reasoning to understand how they have actually applied Article 31(3)(c) of the VCLT to determine *relevant* rules of customary international law. I analyze cases in which courts and tribunals have relied on or rejected the application of customary international law in treaty interpretation, covering various topics in different forums. Although I intend to conduct a fairly comprehensive case law survey and discussion, my primary aim is to cover enough case law to explain the dominant treaty interpretive approach towards using customary international law for IIA interpretation. The purpose of this chapter is not to answer particular controversies but rather to identify more general perspectives, principles, and criteria that require or preclude reliance on customary international law in the interpretative process. Finally, I wrap up by summarizing key points that provide a practical guideline on how rules of customary international law are relevant to the investment treaty interpretation process.

2.2 The International Centre for Settlement of Investment Disputes Convention

A pervasive issue in investment arbitration, with which I am mostly concerned, is the approaches of ISDS tribunals to determine what substantive law governs the merits of investment disputes. This determination has practical consequences for the result of the arbitration and makes the difference between winning or losing the case. By taking this importance into consideration, I intend to examine the extent to which rules of international law imposing environmental obligations on foreign investors would be treated as substantive law to hold foreign investors liable towards environmental protection.

It should be recalled here that since, in this project, I examine the ISDS tribunals that arbitrate under ICSID institutional facilitation and procedural rules, debates on the issue of substantive law have evolved around Article 42(1) of the ICSID Convention. Article 42(1) binds investment arbitrators to govern the merit of disputes by the law chosen by the parties for the resolution of their dispute, or, in the absence of a choice, apply the law of the host State and the rules of international law. Article 42(1) of the ICSID Convention reads:

> The Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law

> of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable.[322]

The first sentence of Article 42(1) requires ISDS tribunals to give the parties full autonomy to choose law applicable to their investment disputes. It provides the parties unlimited freedom to designate the applicable law and requires arbitral tribunals to resolve investor-state disputes based on "such rules of law as may be agreed by the parties." The choice of law could be included in an investment agreement, investment contract, or arbitration *compromis* between parties to an investment dispute. It may contain any national legal system or selected rules of that system, general principles of law, rules common to particular legal systems, international law, or foreign investment treaties.[323] Although there is a possibility that parties to an investment dispute have determined applicable law in an investment contract or include it in an arbitration *compromis*, in most cases, the choice of law clauses are embedded in IIAs themselves out of which investment claims have arisen. Therefore, when investment arbitrations are initiated based on IIAs that contain their own choice of law clauses, investment arbitrators are called on by Article 42(1) to respect such clauses in governing the merits of investment disputes.

For example, IIAs may contain a choice of law clauses that clarifies that the dispute is to be decided "in accordance with the provisions of the Agreement" itself, such that the (public international law) treaty itself is the governing law.[324] Frequently, IIAs state that they are applicable in conjunction with "the principles of international law"[325] or "the applicable rules of international law."[326] For example, Article 1131(1) on the choice of law in the North American

[322] International Centre for Settlement of Investment Disputes (ICSID), *supra* note 64.
[323] Schreuer, *supra* note 180 at 558.
[324] See, e.g., BITs entered into by Argentina, Australia, Belgium and Luxembourg (most BITs with exceptions such as the BIT with Mongolia), Canada, Chile, China (most BITs with exceptions such as the BIT with Australia), Costa Rica, Ecuador, Spain; see also BITs entered into by Bulgaria (with Albania, Ghana, the Slovak Republic), Cuba (with Mexico), the Czech Republic (with Italy, Ireland, Switzerland, Paraguay), Egypt (with Sri Lanka, Uganda), France (with Algeria, the Dominican Republic, Honduras, Hungary, Mexico, Uruguay), Germany (with Kuwait, India, Peru, Zimbabwe), Greece (with Latvia), Italy (with Venezuela), Malaysia (with Vietnam), Mexico (with Portugal), the Netherlands (with Mexico, Venezuela, Zimbabwe), Panama (with Uruguay), Paraguay (Romania), Peru (with Paraguay, Romania), Poland (with Estonia, France, Latvia, Lithuania), Portugal (with Venezuela, Turkey), Switzerland (with Mexico, Paraguay, Peru), United Kingdom (with Lebanon).
[325] See, e.g., BITs entered into by Argentina, Belgium and Luxembourg, Chile, China, Costa Rica, Bulgaria, the Czech Republic, Egypt, Poland, France, Germany, Italy, Panama, Peru.
[326] See, e.g., the BITs entered into between, on the one hand, Canada and, on the other hand, Armenia, Barbados, Croatia, Ecuador, Egypt, Latvia, Lebanon, Panama, Philippines, South Africa, Romania, Thailand, Trinidad and Tobago, Ukraine, Uruguay and Venezuela.

Free Trade Agreement (NAFTA) includes that "[a] Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement"—but note a further basis when that provisions adds "and applicable rules of international law."[327] Likewise, Article 26(6) on the choice of law in the Energy Charter Treaty includes that "[a] Tribunal established under paragraph (4) shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law."[328] The references in these two examples to "applicable rules of international law" is important for the availability of customary international law as law that may be applied in a free-standing way—and not merely as reference points for interpreting the treaty. This is accomplished by the agreement of the parties (first sentence of Article 42(1)) with no need to get into the complex and disputed relationship between a State's domestic law and international law in the second sentence of Article 42(1), to which I now turn.

In its second sentence, which constitutes the central focus of my project, Article 42(1) of the ICSID Convention indicates that in the absence of a choice of law clause in IIAs, which is the case in the majority of IIAs, and if parties to the arbitration have not unequivocally agreed on applicable law in investment contract or an arbitration *compromis*, the "Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable."[329] In this scenario, there is, by definition, no prior agreement on applicable law between the parties, and thus, the law applicable to the merits of the dispute is necessarily the law of the host State and international law, according to the second sentence of Article 42(1). However, contrary to the first situation, in which investor arbitrators have to respect the parties' agreement on the choice of law and interpret their

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[327] *North American Free Trade Agreement (NAFTA), the Government of the United Mexican States and the Government of the United States of America, 17 December 1992, Can TS 1994 No 2 (entered into force 1 January 1994)* (1992), online: <https://wits.worldbank.org/gptad/pdf/archive/nafta.pdf>. The North American Free Trade Agreement (NAFTA) terminated on June 30, 2020 and was replaced on July 1, 2020 by the United Sates – Mexico – Canada Agreement (USMCA), *The United Sates–Mexico-Canada Agreement (USMCA)* (2020), online: <https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement>.

[328] European Energy Charter Conference, *Energy Charter Treaty (ECT)* (1994), online: <https://www.energycharter.org/fileadmin/DocumentsMedia/Legal/1994_ECT.pdf>.

[329] As stated by Gaillard and Banifatemi, "a very large number of BITs do not provide for any choice of law"; Emmanuel Gaillard & Yas Banifatemi, "The Meaning of "and" in Article 42(1), Second Sentence, of the Washington Convention: The Role of International Law in the ICSID Choice of Law Process" (2003) 18:2 ICSID Review 375–411 at 379. They note that the majority of BITs entered into by countries such as the United States, the United Kingdom, France or Germany do not contain a clause on the applicable law regarding investment disputes between one of the contracting States and the investors of the other contracting State.

intention, in the second situation, ISDS tribunals have assumed a margin of power to determine substantive law governing the outcome of disputes—including how national law and international law relate.[330]

Despite the practical importance of substantive law in resolving investment disputes, ambiguities exist over how ISDS tribunals interpret the second sentence of Article 42(1) of the ICSID Convention—i.e. in situations when no mutually agreed choice of law has decided the matter. Such ambiguities result from the fact that two different sets of systemic rules, both national and international law, are stated to be applied in the investment dispute settlement procedures. These ambiguities are further intensified when the text of Article 42(1) bedevils the choice of substantive law in the hands of ISDS tribunals without providing them with guiding principles for determining applicable law. As a result of this, although the majority of ICSID tribunals do not provide, in their awards, explicit expositions on the law applicable to the dispute at hand,[331] their interpretive approach is essentially a choice between:

a) Prioritizing national law and restricting the application of international law to a complementary or corrective role; and

b) Considering roles for both national law and international law to interpret investment treaties, without one prevailing over the other so as to exclude the other altogether.

I will discuss these two traditional and recent interpretive approaches used by ISDS tribunals when referring to the second sentence of Article 42(1) of the ICSID Convention. I first explain how the early approach was to give a certain primacy to national law and only to call international law in when there is no way to avoid it. In this approach, international law was relied upon only in cases of domestic lacunae or where the law of the Contracting States is inconsistent with international law. Second, I discuss how the dominant, more recent, approach has tackled the meaning of "and"—as in, "the law of the Contracting State party… and such rules

[330] The *Ad hoc* Committee of the annulment proceeding in *Wena v. Egypt* clearly notes that "use of the word 'may' in the second sentence of this provision indicates that the Convention does not draw a sharp line for the distinction of the respective scope of international and of domestic law and, correspondingly, that this has the effect to confer on to the Tribunal a certain margin and power for interpretation," *Wena Hotels Limited v Arab Republic of Egypt,* ICSID Case No ARB/98/4, Decision on Application for Annulment 5 February 200*2*, at 941.

[331] Andrew Newcombe & Lluis Paradell, "Applicable Substantive Law and Interpretation" in *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International, 2009) 75.

of international law as may be applicable"—to consider certain roles for both national and international law, without one always prevailing.

2.2.1 Traditional Approach in ISDS Tribunals: Hierarchy of Substantive Law, National, and International

For a long time, ISDS tribunals have looked at the ICSID Convention from the perspective of public international law that ensures state sovereignty is respected. This leads to a perception "that the law of the host State should be given maximum effect has nevertheless been the basis for the theory according to which the applicability of international law should be restricted to cases where the law of the host State contains gaps on particular issues brought before the tribunal or where the law of the host State is inconsistent with international law."[332] This is not simply an assertion of state-law primacy but, it can be argued, follows from a basic premise of public international law itself—that every territorial community may organize itself as a State and, within certain basic limits prescribed by international law, organize its social and economic affairs in ways consistent with its national values. The Declaration on Principles of International Law Concerning Friendly Relations and Co-operation Among States in Accordance with the Charter of the United Nations (Friendly Relations) provides that "[e]ach State has the right freely to choose and develop its political, social, economic and cultural systems."[333] The emphasis here is that the legislative expression of variations in the law of different States is presumptively internationally lawful and entitled to be respected. Accordingly, ISDS tribunals should treat as dispositive the choice of host state law, in cases where Article 42(1) of ICSID applies and, in addition, where the parties do not make a different explicit choice of law in IIAs. In such cases, the law of the State, host to foreign investments, must be applied broadly to the content of investment disputes.

What are the roles of international law beyond being a source of a principle of deference to domestic law that reinforces the reference to host state law in Article 42(1)? Consistent with a public international law perspective of respect for sovereign state choices in economic policy,

[332] Gaillard & Banifatemi, "The Meaning of "and" in Article 42(1), Second Sentence, of the Washington Convention", *supra* note 329 at 381.
[333] United Nations, *Declaration on Principles of International Law concerning Friendly Relations and Cooperation among States in accordance with the Charter of the United Nations* (1971) at 123.

ISDS tribunals may also apply international law in the dispute settlement process to serve either a *complementary* or a *corrective* function. These are not the same. The complementary function means that investment arbitrators might use international law to fill that gap in the case of a gap in the applicable domestic law. This function avoids the question of superiority of one law over the other and treats them as a mutually consistent combination of norms. On the other hand, the corrective function authorizes investment arbitrators to disregard the applicable host state law only when it, or an action taken under it, violates international law. This function proceeds from the fact of an unavoidable conflict between a given national law and a relevant international law rule and opts for the normative paramountcy of international law (versus the other way around). This approach sought to prioritize domestic laws to respect the host State's sovereignty and regulatory autonomy[334] while rendering international law as a "safety net" to ensure fairness and compliance with global standards when domestic law is silent or incompatible with international obligations.[335]

Both of the complementary and corrective functions of international law are acknowledged by the *Ad Hoc* Committee in *Klockner v. Cameroon (1985)*, which other ICSID tribunals or committees later acknowledged:

> Article 42 of the Washington Convention certainly provides that "in the absence of agreement between the parties, the Tribunal shall apply the law of the Contracting State party to the dispute... and such principles of international law as may be applicable." This gives these principles (perhaps omitting cases in which it should be ascertained whether the domestic law conforms to international law) a dual role, that is, complementary (in the case of a "lacuna" in the law of the State), or corrective, should the State's law not conform on all points to the principles of international law. In both cases, the arbitrators may have recourse to the 'principles of international law' only after having inquired into and established the content of the law of the State party to the dispute (which cannot be reduced to one principle, even a basic one) and after having applied the relevant rule of the State's law. Article 42(1) therefore clearly does not allow the arbitrator to base his decision solely on the "rules" or "principles of international law."[336]

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[334] See Katia Yannaca-Small, *Arbitration Under International Investment Agreements* (Oxford University Press, 2018) for discission on how domestic law often governs the investment relationship, as it reflects the sovereign rights of the State to regulate within its territory.
[335] United Nations Conference on Trade and Development (UNCTAD), *Investor-State Disputes: Prevention and Alternatives to Arbitration* (2005).
[336] *Klöckner Industrie-Anlagen GmbH and others v United Republic of Cameroon and Société Camerounaise des Engrais,* ICSID Case No ARB/81/2, First Ad Hoc Committee Decision 3 May 1985, para 69.

Thus, according to *Klockner*, arbitrator needs to establish the domestic law's content an apply the domestic law. Only then does it look to international law, looking for one of three situations, in the following order:

- Is there conformity (or, put another way, convergence) in content of international law? With such full convergence, no further inquiry is needed.
- Does domestic law fail to address the relevant issue (creating a lacuna) that international law can fill, while remaining consistent with domestic law? In combination, there is a "complementarity" of the two systems, each harmonizing with the other.
- If complementarity-based consistency cannot resolve the matter, then this necessarily means a conflict has arisen and one law must displace the other for application in the case. Here, national law is the one that gets displaced at this last-resort stage, with international law serving the "corrective" function.

The reasoning of the *Ad hoc* Committee in *Klockner* is echoed in the decision of the *Ad hoc* Committee in *Amco (1986)*. This committee also notes that, in the absence of an agreement between the parties as to applicable law, the tribunal had to apply both national law and such rules of international law as may be applicable:

> It seems to the ad hoc Committee worth noting that Article 42(1) of the Convention authorizes an ICSID tribunal to apply rules of international law only to fill up lacunae in the applicable domestic law and to ensure precedence to international law norms where the rules of the applicable domestic law are in collision with such norms.[337]

Further, the tribunal in *Autopista v. Venezuela (2003)* explicitly references the complementary and corrective functions of international law, while ambiguously noting that it had heard contentions (presumably from the investor counsel) that international law could play a role that is somehow "beyond" the corrective function:

> The role of international law in ICSID practice is not entirely clear. It is certainly well settled that international law may fill lacunae when national law lacks rules on certain issues (so-called complementary function). It is also established that it may correct the result of the application of national law when the latter violates international law (corrective function). … Whatever the extent of the role that international law plays under

[337] *Amco Asia Corporation and others v. Republic of Indonesia,* ICSID Case No ARB/81/1, First Ad hoc Committee Decision on the Application for Annulment 16 May 1986, para 20.

> Article 42(1) (second sentence), this Tribunal believes that there is no reason, in this case … to go beyond the corrective and supplemental functions of international law.[338]

This approach sheds light on how ISDS tribunals, for nearly twenty years, justified the primacy of host state law in resolving investment disputes and articulated the complementary and corrective functions of international law with respect to sovereign State choice of economic policy. The presumptive primacy of the host state law has been the basis for this approach, according to which the applicability of international law has been restricted to cases where the law of the host State contains gaps on issues brought before ICSID tribunals or where the law of the host State violates international law. One did not, under this understanding, refer directly to international law, apply it, and ignore domestic law (whether it confirmed with international law, whether it had gaps international law could address, or whether it conflicted with international law).

2.2.2 An Emerging Approach in ISDS Tribunals: Different Roles of IIAs, National Law, and International Law

A recent interpretive approach in ISDS tribunals shows that it is no longer the case of national law prevailing over international law initially and then international law coming in only in cases of conflict. Rather, both sources have different roles to play in the investment dispute resolution process that is not captured by the sequencing approach just described. The history of the ICSID Convention proceedings, dominant scholarly literature, and recent case law confirm the re-articulation of the roles of national law and international law under the second sentence of Article 42(1).

2.2.2.1 ICSID Travaux

The history of the ICSID Convention proceedings does not affirm the priority of host state law over international law. Instead, it discloses a consensus of the drafting States that, regardless of the function of the host state law, there is a role for international law as an independent body of substantive rules available to international arbitrators in the second sentence of Article 42(1) of

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[338] *Autopista Concesionada de Venezuela, CA v. Bolivarian Republic of Venezuela,* ICSID Case No ARB/00/5, Award 23 September 2003, para 102.

the ICSID Convention. According to the history of the drafting procedures of the ICSID Convention, the Convention does not support the proposition that international law would be treated as substantive law only when host state law has a lacuna or violates the rules of international law.[339] A close study of the history shows that the main focus of the discussions regarding the second sentence of Article 42(1) was whether, in the absence of an agreement between the parties on the applicable law, international law should constitute an option available to investment arbitrators.

In 1962, international law as a source of law was inserted into the ICSID draft provision on the applicable law: "Arbitral Tribunal shall decide the dispute submitted to it in accordance with such rules of law, whether national or international, as it shall determine to be applicable."[340] Two years later, in 1964, it was made clear in a revised draft that the word "or" was not intended to allow the exclusion of international law through tribunals only applying national law.[341] Thus, the word "and" replaced "or": "[T]he Tribunal shall decide the dispute submitted to it in accordance with such rules of national and international law as it shall determine to be applicable."[342] In 1966, the "and" wording of 1964 Article 42(1) of the Convention draft remained intact such that tribunals now were to "apply the law of the Contracting State party to

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[339] In International Centre for Settlement of Investment Disputes (ICSID), "Summary Record of Proceedings, Addis Ababa Consultative Meetings of Legal Experts, Dec. 16-20, 1963, Document No. 25" in *Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Documents Concerning the Origin and the Formation of the Convention* (Washington, D.C.: International Centre for Settlement of Investment Disputes, 1968) at 267, the Chairman pointed out "that unless the parties had agreed to restrict the competence of the tribunal to determining the validity of the act of expropriation by reference to municipal law, the tribunal could look into municipal law as well as international law. This was the very purpose of going before an international tribunal."

[340] International Centre for Settlement of Investment Disputes (ICSID), "Working Paper in the form of a Draft Convention prepared by the General Counsel and transmitted to the Executive Directors, June 5, 1962, Document No. 6" in *Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Documents Concerning the Origin and the Formation of the Convention* (Washington, D.C.: International Centre for Settlement of Investment Disputes, 1968) at 214.

[341] See also International Centre for Settlement of Investment Disputes (ICSID), "Summary Record of Proceedings, Addis Ababa Consultative Meetings of Legal Experts, Dec. 16-20, 1963, Document No. 25" in *Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Documents Concerning the Origin and the Formation of the Convention* (Washington, D.C.: International Centre for Settlement of Investment Disputes, 1968) at 259 says "The Chairman replied that…the Convention left it to the Tribunal in the absence of a stipulation by the par- ties, to decide whether a claim was subject to national or international law."

[342] International Centre for Settlement of Investment Disputes (ICSID), "Draft Convention: Working Paper for the Legal Committee, Sept. 11, 1964, Document No. 43" in *Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Documents Concerning the Origin and the Formation of the Convention* (Washington, D.C.: International Centre for Settlement of Investment Disputes, 1968) at 630.

the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable)."

Through the course of the drafting, the Chairman of the Legal Committee made it clear that "Article 42 intentionally referred to domestic law and international law since a tribunal might be called upon to determine whether standards set by both systems of law had been respected by the host State."[343] In this process, the question of whether international law plays complementary and corrective functions was not debated as such but were there just under the surface in the arguments put forward by those delegations opposed to the insertion of international law in the draft and seeking to limit its applicability. Indeed, the main focus of the debate on international law was whether or not it should be applied at all. In this context, the new draft that maintained the option of international law was eventually adopted to become the final provision of Article 42(1). It is particularly telling that the Legal Committee expressly choses, in response to the suggestion made by the delegations favoring the subsidiary applicability of international law, not to adopt the inconsistency test: "Mr. Broches (Chairman) then re-stated the principle adopted and explained the *advantages of the present draft over* a text couched in terms whereby international law would become applicable where the domestic legislation of the host State was 'inconsistent' with it."[344] Similarly, the Legal Committee voted against a wording on the basis of the *lacuna/complementarity* test: "Mr. Lokur (India) then requested a vote on a suggestion to limit the application of international law to cases where the domestic legislation of the host State was *silent,* whereupon a vote was taken and the motion defeated by a majority of 19 to 7."[345]

These issues were no longer raised in the following drafts—of Article 45(l) and, later, of Article 42(1)—in which the wording was identical to that of the present Article 42(1) of the Convention. As a result, there is no clear support in the travaux for initial or presumptive priority of national

[343] International Centre for Settlement of Investment Disputes (ICSID), "Memorandum of the Meeting of the Committee of the Whole, Feb. 23, 1965, Document No. 132" in *Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Documents Concerning the Origin and the Formation of the Convention* (Washington, D.C.: International Centre for Settlement of Investment Disputes, 1968) at 985.
[344] International Centre for Settlement of Investment Disputes (ICSID), "Summary Proceedings of the Legal Committee Meeting, December 7, 1964, Document No. 81" in *Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Documents Concerning the Origin and the Formation of the Convention* (Washington, D.C.: International Centre for Settlement of Investment Disputes, 1968) at 804.
[345] *Ibid*.

law over international law or of limiting of the prevailing role of international law to completing or correcting the law of the host State. Instead, "independently of the function it may perform vis-a-vis the law or the host State, there is a role for international law as a mere body of rules available to international arbitrators."[346] The history of ICSID proceedings does not establish host state law as having absolute priority over international law or vice versa. In its place, it demonstrates a new approach where both legal frameworks play substantive roles and work together to resolve disputes.[347]

2.2.2.2 Case Law

ISDS tribunals draw upon three primary sources of substantive law to resolve investment disputes: the investment treaty itself, the law of the host State, and international law.[348] First, investment treaties establish the legal framework for investment protection standards. In investment disputes, foreign investors typically allege that host States have violated these standards, such as fair and equitable treatment or protection against expropriation. Consequently, investment treaties serve as the foundational liability law in the eyes of investment arbitrators.

Second, the host State's domestic law governs the activities and property rights associated with the protected investments. This reflects the host State's sovereign authority to regulate within its territory, including the terms and conditions under which foreign investments operate. Domestic law thus provides the regulatory and legal infrastructure underpinning the investment relationship, ensuring alignment with the host State's policy objectives and public interests.

Third, since investment treaties are international agreements, they inherently invoke the application of international law. Rules and principles of international law, including customary international law, play a critical role in interpreting treaty provisions and resolving disputes.[349]

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[346] Gaillard & Banifatemi, "The Meaning of "and" in Article 42(1), Second Sentence, of the Washington Convention", *supra* note 329 at 403.
[347] Schreuer, *supra* note 180.
[348] Zachary Douglas, "The Hybrid Foundations of Investment Treaty Arbitration" (2003) 74:1 British yearbook of International Law 151–289.
[349] ICSID cases such as the *MTD* award highlighted that "the parties have agreed to this arbitration under the BIT. This instrument being a treaty, the agreement to arbitrate under the BIT requires the Tribunal to apply international law," and that "the breach of an international obligation will need, by definition, to be judged in terms of international law," *MTD Equity SdnBhd& MTD ChileSA v. Chile*, ICSID Case NoARB/0/7, Award 25 May 2004.

These principles ensure consistency with global legal standards and provide a supplementary framework where gaps or ambiguities exist in domestic law or treaty language.

Consequently, the substantive law governing investment disputes is a combination of international law and national law. This combination strikes a balance between treaty obligations, state sovereignty, and international legal norms.

2.2.2.2.1 Role of International Investment Agreement

Investment arbitration claims are first of all based on IIA provisions; they are grounded in the investor's rights and host State's obligations granted by IIAs. IIAs grant foreign investors access to arbitration in order for those investors to be able to claim the substantive protections of the IIA itself. Thus, the substantive provisions of an IIA are the principal applicable law in IIA disputes.[350]

The decision of the Annulment Committee in *Wena v. Egypt (2002)* is the landmark in which, instead of one rule prevailing over another, the tribunal noted that "the use of the word 'may' in the second sentence of this provision [Article 42 of the ICSID Convention] indicates that the Convention does not draw a sharp line for the distinction of the respective scope of international and of domestic law."[351] To examine the meaning of this second sentence and the question of the interrelation between domestic and international law in this context, the Committee explained that both legal orders have a role. The Committee confirmed the primacy of the BIT while adding that "the law of the host State can indeed be applied in conjunction with international law if this is justified. So too international law can be applied by itself if the appropriate rule is found in this other ambit."[352]

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[350] Parra, former Deputy Secretary General of ICSID, writing about the rules of law applicable to the substance of disputes brought under IIAs, confirms this point and states "these mainly have been the rules set out in the substantive provisions of the treaties themselves. In most instances, this follows simply from the investor's invocation of those rules in bringing the claim, such reliance on the rules being explicitly or implicitly authorized by the investor-to-State dispute settlement provisions of the treaty," Antonio R Parra, "Applicable Substantive Law in ICSID Arbitrations Initiated Under Investment Treaties" (2001) 16 ICSID Review - Foreign Investment Law Journal 20 at 21.

[351] *Wena Hotels Limited v. Arab Republic of Egypt,* ICSID Case No. ARB/98/4, Decision on Application for Annulment 5 February 2002, *supra* note 330 para 39.

[352] *Ibid* para 40.

The reasoning of this Annulment Committee is in striking contrast with that of the *Ad hoc* Committee's decision in *Klockner,* according to which "Article 42(1) … clearly does not allow the arbitrator to base his decision *solely* on the 'rules' or 'principles of international law'."[353] Similarly, it contrasts with that of the *Ad hoc* Committee's decision in *Amco,* according to which "Article 42(1) of the Convention authorizes an ICSID tribunal to apply rules of international law *only* to fill up *lacunae* in the applicable domestic law and to ensure precedence to international law norms where the rules of the applicable domestic law are in collision with such norms."[354]

Quite to the contrary, according to the Committee's decision in *Wena,* the tribunal may find two applicable rules in each legal system and yet decide that, under the circumstances of the case, it will apply the rule of international law without any need first to have identified either a *lacuna* in host state law or *inconsistency* between host state and international law. Based on this interpretation, the Committee endorsed the tribunal's primary recourse to the standard of "prompt, adequate, and effective" compensation under the BIT, which could not be achieved through the application of the lease agreements incorporated in Egyptian law.[355]

In relation to the above reference to circumstances of the case, a crucial outcome of the approach taken was to endorse a certain flexibility in such a way that placed considerable discretion in the hands of tribunals as to when and why to decide a case on the basis primarily or even exclusively of international law. As will be seen in the context of the entire reasoning of the tribunal in the boxed-off case note (below), this tribunal-empowering outcome arises from these sentences penned by the Annulment Committee at the second stage of proceedings in *Wena*: "There seems not to be a single answer as to which of these approaches is the correct one. The circumstances of each case may justify one or another solution."

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[353] *Klöckner Industrie-Anlagen GmbH and others v. United Republic of Cameroon and Société Camerounaise des Engrais,* ICSID Case No. ARB/81/2, First Ad Hoc Committee Decision 3 May 1985, *supra* note 336.
[354] *Amco Asia Corporation and others v. Republic of Indonesia,* ICSID Case No ARB/81/1, First Ad hoc Committee Decision on the Application for Annulment 16 May 1986, *supra* note 337 (emphasis added).
[355] *Wena Hotels Limited v. Arab Republic of Egypt,* ICSID Case No. ARB/98/4, Decision on Application for Annulment 5 February 2002, *supra* note 330 para 50.

Wena Hotels Limited v. Arab Republic of Egypt

In 1989 and 1990, Wena Hotels Ltd. ("Wena"), a British company, entered into two long-term lease contracts with the Egyptian Hotels Company ("EHC"), an Egyptian state-owned enterprise responsible for managing and operating hotels in Egypt, for the development of two hotels by Wena for 25 years. However, shortly after entering into the contracts, EHC and Wena disputed about their respective obligations as a result of which, on 1 April 1991, EHC took possession of both hotels by force. In early 1992, the Chief Prosecutor of Egypt ruled that the seizure of the hotels had been illegal. This decision required EHC to return control of the hotels to Wena. When Wena regained control of the hotels, they found the properties in a significantly damaged condition. The damage was attributed to the period during which EHC had seized and managed the hotels, allegedly failing to maintain them properly.
After the return of the hotels, Wena sought compensation from Egypt, through the actions of its state-owned enterprise (EHC), as the damages affected Wena's ability to operate the hotels profitably and recover their investment. In 1998, Wena initiated ICSID arbitral proceedings against Egypt under the provisions of the Agreement for the Promotion and Protection of Investments entered into by the United Kingdom and Egypt (IPPA) claiming that Egypt's actions constituted an unlawful expropriation without "prompt, adequate and effective compensation" and that Egypt had failed to accord Wena's investments "fair and equitable treatment" and "full protection and security," as required by the BIT.

On December 8, 2000, the tribunal applied the BIT as the primary source of substantive law. And since there was no special agreement between the parties on the applicable law (the BIT itself did not have one and there was also no separate choice of law agreement), the tribunal subsidiarily applied both Egyptian law and international law, in accordance with the second sentence of Article 42(1) of the ICSID Convention, without determining the hierarchy between these two sources. The tribunal agreed with Wena that Egypt had failed to accord Wena's investment "fair and equitable treatment" and "full protection and security" in violation of the BIT. The tribunal also agreed with Wena that Egypt's actions constituted an expropriation without "prompt, adequate and effective compensation" in violation of the BIT.

On January 2001, Egypt filed with the ICSID tribunal an application for the annulment of the arbitral award rendered on December 8, 2000, in the arbitration proceeding between Wena and Egypt. The application for annulment was based on the tribunal's alleged failure to apply Egyptian law, as adequate substantive law, in contravention of Article 42(1) of the ICSID Convention. Egypt noted that the lease contracts were concluded between Wena and EHC. And since two leases were subject to Egyptian law, the tribunal was under the obligation to apply such law, in accordance with the choice of law required by the first sentence of Article 42(1).[356] Wena argued in response that the parties to this case made no choice of law under Article 42(1).[357] It believed Egyptian law was indeed applicable, but only in the context of the disputes concerning those parties (Wena and EHC) that involved the commercial aspects specifically arising from the lease contracts. The dispute before the tribunal involved different parties, namely the investor and the Egyptian State, and concerned a subject matter entirely different from the commercial aspects under the lease contracts. In the Wena's view, the investment dispute is about the role of the State in the light of its obligations under the IPPA.

The Annulment Committee confirmed that there is a connection between the leases and the IPPA: "the former were designed to operate under the protection of the IPPA as the materialization of the investment."[358] But "just as EHC does not represent the State nor can its acts be attributed to it because of its commercial and private function, the acts or failures to act of the State cannot be considered as a question connected to the performance of the parties under the leases."[359] The leases deal with questions that are by definition of a commercial nature. The IPPA deals with questions that are essentially of a governmental nature, namely the standards of treatment accorded by the State to foreign investors. Thus "the private and public functions of these various instruments are thus kept separate and distinct."[360] "This Committee accordingly concludes that the subject matter of the lease agreements submitted to

[356] *Ibid* para 28.
[357] *Ibid* para 29.
[358] *Ibid* para 35.
[359] *Ibid* para 35.
[360] *Ibid* para 35.

Egyptian law was different from the subject matter brought before ICSID arbitration under the IPPA."[361]

It follows that it cannot be held that the parties to this case made a choice of law under the first sentence of Article 42(1) of the ICSID Convention. Thus, with respect to the second sentence of Article 42(1) of the ICSID Convention, the Annulment Committee had to examine the interrelation between domestic and international law. For this purpose, the Committee recalled the various views expressed as to the role of national law and international law in the context of Article 42(1):

> Some views have argued for a broad role of international law, including not only the rules embodied in treaties but also the rather large definition of sources contained in Article 38(1) of the Statute of the International Court of Justice. Other views have expressed that international law is called in to supplement the applicable domestic law in case of the existence of *lacunae.* In *Klockner I* the *ad hoc* Committee introduced the concept of international law as *complementary* to the applicable law in case of *lacunae* and as *corrective* in case that the applicable domestic law would not conform on all points to the principles of international law. There is also the view that international law has a controlling function of domestic applicable law to the extent that there is a collision between such law and fundamental norms of international law embodied in the concept of *jus cogens.* Some of these views have in common the fact that they are aimed at restricting the role of international law and highlighting that of the law of the host State. Conversely, the view that calls for a broad application of international law aims at restricting the role of the law of the host State. There seems not to be a single answer as to which of these approaches is the correct one. The circumstances of each case may justify one or another solution.[362]

The Annulment Committee, however, noted that "the use of the word 'may' in the second sentence of this provision [Article 42 of the ICSID Convention] indicates that the Convention does not draw a sharp line for the distinction of the respective scope of international and of domestic law."[363] It confirmed that "the law of the host State can indeed be applied in conjunction with international law if this is justified. So too international law can be applied by itself if the appropriate rule is found in this other ambit."[364] In this context it cannot be concluded that the resort to the rules of international law under the Convention, or under

[361] *Ibid* para 36.
[362] *Ibid* para 38.
[363] *Ibid* para 39.
[364] *Ibid* para 40.

particular treaties related to its operation, is antagonistic to that State's national interest. Therefore, "the reliance of the Tribunal on the IPPA as the primary source of law is not in derogation or contradiction to the Egyptian law and policy in this matter. In fact, Egyptian law and investment policies are fully supportive of the rights of investors in that country. The ICSID Convention and the related bilateral investment treaties are specifically mentioned in Egypt's foreign investment policy statements."[365] The Committee concluded that, in applying the rules of the IPPA in the instant case, the tribunal did not fail to apply adequate substantive law.

The tribunal in *CMS Gas Transmission Company v. Argentina (2005)* also noted the multiplicity of substantive law in the dispute settlement process. The parties in this case had not chosen a particular law applicable to the resolution of the investment dispute. In the absence of such choice, the second sentence of Article 42(1) of the Convention was the rule governing the determination of the law to be applied by the tribunal. However, similar to *Wena*, the parties in this case expressed radically different views.

The claimant argued "that only the Treaty and international law are applicable to the dispute while the law of the host State plays only a marginal role, relevant only as a matter of fact."[366] On this basis, the claimant asserted that Argentine law is relevant only in the context of factual matters, such as with regard to the nature of the assurances made to CMS. The respondent, however, invoked the application of the Argentine Constitution. It is explained that "the protection of the right of property enshrined in the Constitution has been interpreted by the Courts as not having an absolute character and that State intervention in the regulation of individual rights is justified, provided such intervention is both legal and reasonable when factoring in social needs."[367] Despite these different views, the tribunal repeated the structure of Article 42(1) by concluding that "in the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on conflict of laws) and such

[365] *Ibid* para 45.
[366] *CMS Gas Transmission Company v. The Argentine Republic,* ICSID Case No ARB/01/8, Award 12 May 2005, para 109.
[367] *Ibid* para 113.

rules of international law as may be applicable."[368] By referring to the Annulment Committee in *Wena v. Egypt*, the tribunal noted that, although much discussion has surrounded the meaning of Article 42(1) of the Convention and the restricted application of international law in a complementary or corrective role, "a more pragmatic and less doctrinaire approach has emerged, allowing for the application of both domestic law and international law if the specific facts of the dispute so justifies. It is no longer the case of one prevailing over the other and excluding it altogether. Rather, both sources have a role to play."[369] The tribunal then rightly found that there is a close interaction between national law and international law and thus these rules are inseparable and will, to the extent justified, be applied by the tribunal.

In the aforementioned cases, although IIAs are considered as the primary source to articulate investors' rights and host States' responsibilities, the tribunals noted that domestic law and international law must be applied jointly and harmoniously to the substance of the investment disputes.[370] However, these tribunals remain silent on how different sources of substantive law must be applied in such a way that none of them nullifies the others—which silence underlines the point made earlier about how this more flexible approach is also at the same time one that empowers tribunals as 'the circumstances of each case' decision-makers.[371] The discussion that follows will explore the practical implications of applying both national law and international law in ISDS tribunals.

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[368] *Ibid* para 108.
[369] *Ibid* para 115.
[370] This point is clearly mentioned in the proceeding of the *Asian Agricultural Products Ltd. (AAPL) v. Republic of Sri Lanka*: "the Bilateral Investment Treaty is not a self-contained closed legal system limited to provide for substantive material rules of direct applicability, but it has to be envisaged within a wider juridical context in which rules from other sources are integrated through implied incorporation methods or by direct reference to certain supplementary rules, whether of international law character or of domestic law nature," *Asian Agricultural Products Ltd. (AAPL) v. Republic of Sri Lanka,* ICSID Case No. ARB/87/3, Award 27 Jun 1990, para 20.
[371] Likewise, in *Urbaser*, the tribunals explained that that it must first apply the BIT. But it further said: "A BIT is not a set of self-contained rules" and "this entails applying not only the BIT, but also international law in general." The tribunal "must [also] apply the law of the Argentine Republic."[371] The tribunal notes that Article X(5) of the BIT clearly states the principle that the claims submitted to this tribunal are to be decided on the basis of the provisions of the BIT. This does not exclude, however, that certain particular matters that are relevant to the requirements related to claims brought under the BIT have to be determined in conjunction with ("and") other sources of law, as they are mentioned in Article X(5) and declared to be applicable "where appropriate." It may also be noted that on certain particular items, the BIT refers to national law, *i.e.* relating to the content and scope of the rights corresponding to the various categories of assets (Art. 1(2)), and in referring to "investments in accordance with the legislation of the country receiving the investment," which means the domestic law of the state party where the investment has been made (Art. 11(1), HI(l), V). It also refers to matters governed by general international law (Art. VII(l)).

2.2.2.2.2 The Role of National Law in Relation to the Timing of Investment Disputes and Disputes Arising from Investments

In relation to the second sentence of Article 42 of the ICSID Convention, in practice, the law of the contracting state parties has been interpreted by tribunals relatively narrowly to impose obligations on investors only at the time they made their investments.[372] Despite the lack of any specifications for the role of national law in the investment dispute resolution process, national law is often being applied as substantive law to examine the existence of the investment protected by investment agreements.[373] Even in cases where jurisdiction is limited to claims alleging the violation of a treaty's substantive standards, an incidental application of domestic law is often called for. The most obvious situation of this kind arises where there is a dispute about the existence of rights that the investor seeks to protect. Whether these rights are property rights, rights arising from contracts, or other intangible rights, they typically exist by virtue of a domestic legal system. Indeed, when disputes involve questions about the legal existence or scope of the investment, tribunals often defer to host states law. The preliminary question of the existence of the rights in dispute cannot be answered without resort to a domestic system of law, most often the host State's law. This reliance reflects States' sovereign authority to define and regulate property and economic activities within their territory.[374]

As argued by Douglas, "[i]nvestments disputes are about investments, investments are about property, and property is about specific rights over things cognisable by the municipal law of the host state."[375] That is, whether a particular right, interest or asset held in the territory of a State party to an IIA is an investment protected by the IIA is a matter for the IIA not municipal law; but "in order for a particular asset to be able to qualify as an investment under the IIA, it must first exist and such existence is owed to the law of the territory in which such asset is allegedly held."[376] Thus, while IIAs designate which assets are to be considered investments for the

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[372] Jean-Michel Marcoux, *International Investment Law and Globalization: Foreign Investment, Responsibilities and Intergovernmental Organizations* (Routledge, 2008); Rahim Moloo & Alex Khachaturian, "The Compliance with the Law Requirement in International Investment Law" (2011) 34 Fordham International Law Journal 1472.
[373] Andrea K Bjorklund, "Applicable Law in International Investment Disputes" in Chiara Giorgetti, ed, *Litigating International Investment Disputes: A Practitioner's Guide* (Brill | Nijhoff, 2014) 261.
[374] See Rudolf Dolzer & Christoph Schreuer, *Principles of International Investment Law* (Oxford University Press, 2012) for discussion on the role of host state law in determining the legality of investments.
[375] Douglas, *supra* note 348 at 197.
[376] Newcombe & Paradell, *supra* note 331 at 93.

purposes of the treaty, the preliminary question as to whether one of these types of investments exists is a matter primarily for the municipal law of the host State, not international law. Some IIAs make this role explicit. For example, Article I (2) of Argentina-Spain (1991) provides: "The content and scope of the rights corresponding to the various categories of assets shall be determined by the laws and regulations of the Party in whose territory the investment is situated."[377] In different words, Article 1(a) of Argentina-UK (1990) provides "'Investment' means every kind of asset defined in accordance with the laws and regulations of the Contracting Party in whose territory the investment is made."[378] Other IIAs, like Bolivia-France (1989), make the same point by adding to the definition of protected investments a provision that investments must be duly made in accordance with the national law of the host State.[379] This does not mean that host state law determines or limits what qualifies as an investment for the purposes of the IIA. Rather, the existence of the asset that may qualify as an investment under the IIA, as well as its validity, is a matter of domestic law.

In a more practical context, *Desert Line Projects LLC v. Yemen (2008)* case is a clear example thereby the ISDS tribunal considered the role of national law in examining the existence of the investment and determining whether the investment activity is unlawful in order to disqualify it from protection under the BIT.[380] In this case, although the tribunal admitted the application of the national law in the dispute settlement process, it was not satisfied by the host State's claim to that the application of national law rendered the investment non-existent due to its lack of compliance with national law.

[377] note 113.
[378] *Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the Promotion and Protection of Investments* (1990), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bit/161/argentina---united-kingdom-bit-1990->.
[379] *Agreement between the Government of the French Republic and the Government of the Republic of Bolivia on the Reciprocal Encouragement and Protection of Investments* (1989), online: <https://edit.wti.org/document/show/4f01b204-37cb-459b-b146-394bfda1931d>.
[380] *Desert Line Projects LLC v. Republic of Yemen,* ICSID Case No ARB/05/17, Award 6 February 2008.

Desert Line Projects LLC v. Republic of Yemen

Beginning in 1997, DLP Company, as a private contractor, contracted with the government of Yemen to coordinate with Yemeni authorities for designing, constructing, and completing the asphalt roads. Several years later, in 2004, Yemen disagreed with DLP about the amount of work completed and then threatened DLP's personnel with automatic weapons at DLP's worksites and suspended all work pending payment. This created a hostile work environment, increasing safety concerns and operational delays, and caused significant financial consequences for DLP.

DLP then sought recourse through dispute resolution mechanisms and initiated a claim before an ISDS tribunal alleging that Yemen violated the Oman-Yemen BIT (1998), in particular it failed to provide the investment with "fair and equitable treatment" standard under Article 3 of the BIT: "The two Contracting Parties undertake to ensure fair and equitable treatment to the investments of investors of the other Contracting Party." In its defence, Yemen argued that the investment was never "accepted" by the host State and that no investment certificate was issued, both being requirements under Article 1(1) of the BIT.[381] The investment was thus rendered unlawful with respect to national law of the host State and thus is not entitled to be protected under the BIT, Yemen argued. Yemen referred to Article 1(1) of the BIT, which says:

> The term "Investment" shall mean every kind of assets owned and invested by an investor of one Contracting Party, in the territory of the other Contracting Party, and that is accepted, by the host Party, as an investment according to its laws and regulations, and for which an investment certificate is issued.
> The term "Investment" includes in particular, though not exclusively:
> a) Movable and immovable property as well as other guarantees pertaining to it such as mortgages, preferred debts and other liens.
> b) Securities, stocks, shares and company's bonds.
> c) Debts as well as service of debt deriving from a contract related to the investment.
> d) Intellectual and industrial property rights and intangible elements relating to commercial assets such as trademarks, copyrights, designs, goodwill, etc. used in a licensed investment.

[381] Desert *Line Projects LLC v Republic of Yemen,* ICSID Case No ARB/05/17, Award 6 February 2008, para 92.

e) Concessions conferred according to the host country's applicable laws including rights to extract, exploit and search for natural resources that give its beneficiaries an appearance of legitimacy during the licensed period.

To examine the host State's objections, the tribunal confirmed the role of national law in evaluating whether the DLP investment is lawful in order to be protected by the BIT. The tribunal further explained that the phrase "according to its laws and regulations" in Article 1(1) demonstrates the role of national law to qualify the words *accepted* and *investment*. However, it noted that the respondent has not adduced any expert evidence of Yemeni law to assist the tribunal in its understanding of the key concepts of "accepted" and "certificate":

> The Respondent has not sought to show that these concepts have any special meaning in Yemeni law that might deviate from the plain-language purport of the terms "accepted" and "certificate." Nor has the Respondent called a single witness to explain the factual circumstances relevant to the understandings between the Claimant and the many high officials who were concerned with the conception, negotiation, and performance of the Claimant's project. Given its position as author of the objection, the Respondent must accept the consequences of its forensic choices.[382]

The tribunal had not been directed to any explicit provision in the national law that would require a particular form in which an investment must be "accepted," or to preclude that the highest organs of the State choose their own manner of "acceptance." Nor had the arbitrators been shown any Yemeni definition of "investment" which would override the definitions of the BIT itself. Thus, the objection to the effect that the claimant's investment was never "'accepted by [the Respondent] as an investment according to its laws and regulations' is as unpersuasive as it is unattractive."[383]

To explain the role of national law in determining the existence of investment, the tribunal added that "in State practice in the BIT area, the phrase 'according to its laws and regulations' is quite familiar. Moreover, it has been well traversed by arbitral precedents, notably the *Inceysa* case and the *Fraport* case, which make clear that such references are intended to ensure the legality of the investment by excluding investments made in breach of fundamental principles of the host State's law, e.g. by fraudulent misrepresentations or the dissimulation of

[382] *Ibid* para 98.
[383] *Ibid* para 99.

true ownership."[384] The tribunal raised the decision of ICSID tribunal in *ESI SpA et Astaldi SpA v. Algeria* case that said:

> the mention in the text of conformity to laws and regulations in vigour does not constitute a formal acknowledgement of the notion of investment as understood in Algerian law in a restrictive fashion, but rather, adopting a classic and wholly justified formulation, the loss of protection suffered by any investments made in violation of fundamental governing principles.[385]

The tribunal then concluded that, under these circumstances, Yemen had not come close to satisfying the tribunal that the claimant made an investment which was either inconsistent with Yemeni laws or regulations or failed to achieve acceptance by the respondent. The tribunal held that the conduct of the respondent amounted to a breach of Article 3 of the BIT.[386]

Accordingly, the *Desert Line Projects LLC v. Yemen* case is a revealing example of how ISDS tribunals often interpret the law of host States narrowly when focusing on the obligations that investors were required to fulfill at the time of making their investment. This means that the legality of the investment is assessed based on whether it complied with the host State's law at the time it was initiated, during the establishment, (e.g., obtaining necessary permits or adhering to regulations) in a way that is of a most-favourable-to-the-investor sort. In any case, returning to the use of national law serves only to look at the law at the time of investment to know whether the investment exists. The basic point is that this is where the use of national law (however interpreted) stops: tribunals generally do not extend the obligations under host state law to the investor's ongoing conduct after the investment is established unless explicitly stated in the investment agreement. This arises the question of post-establishment illegal conduct by investors *under international law* on which this dissertation focuses, notably in the case study of Chapter 4.

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[384] *Ibid* para 104.
[385] *LESI, S.pA and Astaldi, S.pA v People's Democratic Republic of Algeria,* ICSID Case No ARB/05/3, Decision on Jurisdiction 12 July 2006, para 83 (translated from French).
[386] *Desert Line Projects LLC v. Republic of Yemen, ICSID Case No. ARB/05/17, Award 6 February 2008*, *supra* note 380 para 193.

2.2.2.2.3 Role of International Law

International rules, beyond those clearly expressed in the treaty text of IIAs themselves, are often applied in ISDS tribunals as *liability law* to first determine whether host States have incurred international responsibility towards foreign investors by breaching IIAs and, secondly, to establish the legal consequences of IIA violations, such as reparation in various forms and compensation. The issue of the responsibility of host States for measures breaching IIAs is a matter for international law, not domestic law. Thus, although domestic law is relevant to determine the existence and scope of the investment, IIA violations need to be analyzed through the lens of international law. By dint of Article 27 of the VCLT that says "a party may not invoke the provisions of its internal law as justification for its failure to perform a treaty"[387] and of Article 3 of the International Law Commission (ILC) Articles on State Responsibility—"the characterization of an act of a State as internationally wrongful is governed by international law. Such characterization is not affected by the characterization of the same act as lawful by internal law"—ISDS tribunals must assess host states conduct against the standards of protection in IIA and international law.[388]

It should be noted here that, although "liability" (and thus liability law) is conceived in public international law or some of its branches as a secondary-rule consequence of breach of primary obligations, in much (municipal) civil law usage, liability also refer to the condition produced by a breach of a (primary) obligation—similar to the state of legal affairs arising after judicial finding of such breach. Such state of legal affairs includes the remedial consequences of having breached a primary obligation. In that sense, "liability"—in my usage in this dissertation—functions both like the notion of "responsibility" in the law of state responsibility (that is, as an intermediate juridical condition between identification of primary/substantive obligation and remedial obligations once a breach has been determined) and as including the remedial consequences (as in, that which one is liable to do to repair the harm). It is this combination—breach of international legal obligation and remedial consequences—that I will refer to as liability law in this dissertation, notably in Chapter 4.

[387] *Supra* note 4 Article 27.
[388] International Law Commission (ILC), *supra* note 214 Article 3.

I also prefer the term liability law in order to distinguish this from the public international law "responsibility law" (law of state responsibility) in order to capture a notion of legal accountability that is tortious in nature in a way not captured by notions of public-law responsibility and in a way that echoes municipal-law uses of the term "liability" (e.g., product liability law) in the private law of tort. Further, by way of extension of domestic-law usage for lawsuits seeking compensation, "liability" also suits litigation contexts—including the ISDS litigation context. "Responsibility" remains the accepted and preferred term for state conduct (including state conduct that in relation either to failure to prevent harm by non-state actors or to the direct imputation of non-state acts to the state on principles of agency). But, where law is either applicable only to the non-state actors or to state and non-state actors alike as a hybrid collection of actors (where there is no pure agency involved), a term like "liability" suits the transnational/transnationalized nature of the law. At the same time, I may not have always used it consistently, so I should make clear that, even when a sentence may seem to indicate "liability law" is being used to refer to the primary rules, I mean ultimately the substantive obligations, the liability attached to breach of such obligations, and, from there, the particular remedial (or other) consequences of being in breach. Put yet another way, "liability law" encompasses the amalgam of substantive/primary and secondary rules (the substantive obligations, attribution rules, determination of breach, remedies, defence, and so on).

The decision of the Annulment Committee in the *Azurix Corp. v. Argentine Republic (2006)* case highlights an ongoing debate surrounding the second sentence of Article 42(1) of the ICSID Convention. The *Azurix* decision serves as a prominent example of how an ISDS tribunal can comprehensively address the interaction between these two legal frameworks—between national law and international law. The Annulment Committee examined this interplay by referencing leading cases, offering clarity on the application and boundaries of both national and international law in resolving disputes in ISDS tribunals.

Azurix Corp v. The Argentine Republic, Decision on Annulment

Recall this case, already discussed in Chapter 1 with respect to the initial decision; I now look at the issues and arguments of the annulment proceedings. By way of reminder as to what the case was about, Azurix Corporation, a U.S.-based company owned by Enron, secured a 30-year concession in Buenos Aires for water services but faced governmental complaints and contract termination in 2001. In response, Azurix initiated an ICSID arbitration against Argentina, claiming expropriation and breach of fair and equitable treatment under the Argentina-U.S. BIT. On July 14, 2006, the tribunal ruled against Argentina, holding it liable for failing to protect Azurix's investment and taking arbitrary measures.[389]

On November 13, 2006, Argentina filed an application for annulment of the tribunal's award on July 14, 2006, citing among other grounds for annulment issues relating to the tribunal's failure to apply the law of Argentina to disputed issues arising out of the Concession Agreement. Argentina argued that the tribunal manifestly exceeded its powers by not considering the second sentence of Article 42(1) of the ICSID Convention that requires a tribunal to decide the dispute in accordance with "the law of the Contracting State party to the dispute ... and such rules of international law as may be applicable." Argentina said, as the parties did not agree on the applicable law, the tribunal was obliged, in accordance with Article 42 of the ICSID Convention, to apply Argentine law and international law "as may be applicable." It further added, in accordance with this Article, the dispute is basically governed by Argentine law, which is also applicable to contractual matters and provincial administrative law underlying the claim.

However, despite the wording of the Article, the tribunal, in its initial award concluded that "the Tribunal's inquiry is governed by the ICSID Convention, by the BIT and by applicable international law."[390] Argentina added that the tribunal determined the disputed

[389] For a comprehensive discussion, see Chapter 1, *supra*, 1.2.3.2.3.
[390] *Azurix Corp. v. The Argentine Republic, ICSID Case No. ARB/01/12, Award 14 July 2006*, *supra* note 233 para 62.

issues arising out of the Concession Agreement on the basis that they were of a "factual nature."[391] Thus the tribunal referred to what it considered to be Argentine law in a section of the Award dealing with the "Facts" and proceeded to determine the disputed issues arising out of the Concession Agreement on the basis that they were of a "factual nature."[94] Argentina then argued that the tribunal could not avoid the application of Argentine law as the governing law of the contract by re-labelling issues of contractual interpretation as issues of fact. Even if, in general international law, a national law "is generally regarded as a fact with reference to which rules of international law have to be applied," under Article 42(1) of the ICSID Convention, national law has to be treated as part of the applicable law and not as a fact.[392] Argentina pointed out that although the tribunal did not completely discard Argentine law, insofar as "the law of Argentina should be helpful in the carrying out of the Tribunal's inquiry into the alleged breaches of the Concession Agreement to which Argentina's law applies,"[90] the tribunal stated that this inquiry should be limited because of "the treaty nature of the claims under consideration."[91] Argentina concluded that the tribunal thereby disregarded Argentine law in deciding the controversy because it found that Argentine law may be used to inquire into the alleged breaches of the Concession Agreement by the parties by the investor, while nonetheless finding that such breaches of the Concession Agreement were not part of the "claims under consideration."[393] As such, Argentine law was not truly considered by the tribunal to be applicable law to the claims under consideration, contrary to Article 42(1).

In the annulment proceedings, Azurix noted that, under Argentine law, international treaties have primacy over domestic laws, and that the tribunal would apply "both legal orders" since each one had "a role to play" which "may vary depending on which element of the dispute is considered."[394] The tribunal applied the BIT, the ICSID Convention, international law and Argentine law to consider Azurix's claims, applying each of them in its proper role. Argentine law was applied, for instance, to the claims related to the zoning, coefficients, and construction

[391] *Azurix Corp v. The Argentine Republic,* ICSID Case No ARB/01/12, Decision on Annulment 1 September 2009, para 132.
[392] *Ibid* para 134.
[393] *Azurix Corp. v. The Argentine Republic, ICSID Case No. ARB/01/12, Award 14 July 2006*, *supra* note 233 para 67.
[394] *Azurix Corp. v. The Argentine Republic,* ICSID Case No. ARB/01/12, Decision on Annulment 1 September 2009, *supra* note 391 para 135.

variations by means of which the tribunal arrived at the conclusion that the Province's conduct not only violated the Concession Agreement and the national-law regulatory framework but also was an exercise of sovereign power that violated BIT standards.[395] Azurix then explained that international law was then correctly applied by the tribunal to determine whether the provisions of the BIT had been violated. To further highlight Azurix's support for the tribunal's decision, it should be noted that in the initial claim, the Azirux referred, among others, to Professor Weil's opinion that: "the existence of a Bilateral Investment Treaty raises the question of compliance with the rights and obligations contained therein to the level of a matter under international law, with respect not only to relations between the States parties to the treaty *but also to relations between the host State and the investor.*"[396] It said that the BIT requires "the Argentine Republic to afford U.S. investors like Azurix treatment no less favorable than that required by international law, both with respect to investment generally, and in particular with respect to expropriations or measures tantamount to expropriation of an investment."[397] The claimant relied again on Professor Weil's opinion that "no matter how domestic and international law are combined, under the second sentence of Article 42(1), international law always gains the upper hand and ultimately prevails. It prevails indirectly through the application of domestic law where the latter is deemed consistent with international law or incorporates it. It prevails directly where domestic law is deemed deficient or contrary to international law. Thus, under the second sentence of Article 42(1), international law has the last word in all circumstances: international law is fully applicable and to classify its role as 'only' 'supplemental and corrective' seems a distinction without a difference."[398] On the basis of these arguments, Azurix concluded that the approach of the tribunal is consistent with international practice, that the tribunal was justified in applying the BIT and international law to Azurix's claims under the BIT.

The Annulment Committee upheld the tribunal's ward that the law applicable under Article 42 of the ICSID Convention to Azurix's claims of breaches of the BIT is the ICSID Convention,

[395] *Ibid* para 135.
[396] *Azurix Corp. v. The Argentine Republic, ICSID Case No. ARB/01/12, Award 14 July 2006*, *supra* note 233 para 59.
[397] *Ibid* para 59.
[398] *Ibid* para 61.

the BIT and applicable international law, finding no serious procedural or substantive errors. The Annulment Committee raised the point that under the second sentence of Article 42(1) both legal orders have a role to play, which role will depend on the nature of the dispute and may vary depending on which element of the dispute is considered. It then highlighted that this point was taken into consideration for the several times by the tribunal for its Award issued on July 14, 2006. At paragraph 65 of the Award, the tribunal began by noting *"the agreement of the parties with t*he statement that the BIT is the point of reference for judging the merits of Azurix's claim."[399] At paragraph 66, the tribunal noted: Article 42(1) has been the subject of controversy on the respective roles of municipal law and international law," and stated that "both legal orders have a role to play, which role will depend on the nature of the dispute and may vary depending on which element of the dispute is considered."[400] To render its Award, the tribunal also referred to the Annulment Committee in *Wena v. Egypt* considered that "[t]he law of the host State can indeed be applied in conjunction with international law if this is justified. So too international law can be applied by itself if the appropriate rule is found in this other ambit."[401]At paragraph 67 of the Award, the tribunal referenced the Annulment Committee in *Vivendi II* several times to note that a "Tribunal's inquiry is governed by the ICSID Convention, by the BIT and by applicable international law."[402]

The Annulment Committee in Azurix also referred further to the Annulment Committee in *Vivendi II*, which said:

> As to the relation between breach of contract and breach of treaty in the present case, it must be stressed that Articles 3 and 5 of the BIT do not relate directly to breach of a municipal contract. Rather they set an independent standard. A state may breach a treaty without breaching a contract, and vice versa, and this is certainly true of these provisions of the BIT. The point is made clear in Article 3 of the ILC Articles, which is entitled "Characterization of an act of a State as internationally wrongful":
> The characterization of an act of a State as internationally wrongful is governed by international law. Such characterization is not affected by the characterization of the same act as lawful by internal law. In accordance with this general principle (which is undoubtedly declaratory of general international law), whether there has been a breach of the BIT and whether there has been a breach of contract are different questions. Each of these claims will be determined by reference to its own proper or

[399] *Ibid* para 65.
[400] *Ibid* para 66.
[401] *Ibid* para 66.
[402] *Ibid* para 67.

> applicable law—in the case of the BIT, by international law; in the case of the Concession Contract, by the proper law of the contract, in other words, the law of Tucumán. For example, in the case of a claim based on a treaty, international law rules of attribution apply, with the result that the state of Argentina is internationally responsible for the acts of its provincial authorities. By contrast, the state of Argentina is not liable for the performance of contracts entered into by Tucumán, which possesses separate legal personality under its own law and is responsible for the performance of its own contracts.[403]

The Annulment committee in the *Vivendi II* Annulment Decision went on to quote from the judgment in the *ELSI* case, in which the ICJ said:

> Compliance with municipal law and compliance with the provisions of a treaty are different questions. What is a breach of treaty may be lawful in the municipal law and what is unlawful in the municipal law may be wholly innocent of violation of a treaty provision. ... [T]he fact that an act of a public authority may have been unlawful in municipal law does not necessarily mean that that act was unlawful in international law, as a breach of treaty or otherwise. A finding of the local courts that an act was unlawful may well be relevant to an argument that it was also arbitrary; but by itself, and without more, unlawfulness cannot be said to amount to arbitrariness... Nor does it follow from a finding by a municipal court that an act was unjustified, or unreasonable, or arbitrary, that that act is necessarily to be classed as arbitrary in international law, though the qualification given to the impugned act by a municipal authority may be a valuable indication.[404]

The Annulment Committee in *Azurix* then agreed with these findings in the *Vivendi II* Annulment Decision and the *ELSI* case and confirmed that the claims brough by Azurix must therefore be determined not through the application of the municipal law of any State but through the application of the terms of the treaty to the facts of the case in accordance with general principles of international law. The Annulment Committee in Azurix therefore found no fault with the tribunal's identification of the applicable law under Article 42. For these reasons, the Committee rejected Argentina's ground of annulment under Article 52(1)(b) based on the alleged failure of the tribunal to apply the applicable law under Article 42 of the ICSID Convention.

[403] *Compañia de Aguas del Aconquija SA and Vivendi Universal v. Argentine Republic,* ICSID Case No ARB/97/3, Decision on Annulment, 3 July 2002, para 97.
[404] para 73.

2.2.2.3 Interaction between Rules of International Law

Interaction between rules of international law is a central issue that must be discussed to understand how ISDS tribunals determine substantive law under the second sentence of Article 42(1) of the ICSD Convention. Notwithstanding the substantial implications of managing interaction between rules of international law for the outcome of investment disputes, the ICSID Convention is silent on the scope of rules of international law that could be considered as the law governing the substantive aspects of disputes. This leaves ISDS tribunals with an enormous discretion that may result in contradictory interpretive approach: almost any rule of international law could resolve substantive aspects of investment disputes (extensive interpretation)[405] , or none of the rules of international law beyond investment treaties could resolve substantive aspects of investment disputes (restrictive interpretation).[406]

This difference in the interpretive approach amongst ISDS tribunals stems from the way they engage with the Article 31(3)(c) of VCLT that states international treaties are "governed by international law" and must be interpreted inter alia in the light of "any relevant rules of international law applicable in the relations between the parties." Therefore, ISDS tribunals must determine the liability of host States by applying the specific terms of IIAs under which the claim is brought in light of the interpretive effects of other sources of international law that are set out in Article 38 of the Statute of the International Court of Justice: international conventions, whether general or particular; international custom; the general principles of law recognized by civilized nations; and judicial decisions and teachings of the most highly qualified publicists.

[405] Eckart Klein, *Self-Contained Regime* (Oxford University Press, 2006) Max Planck Encyclopedia of Public International Law. Scholars like Dupuy also argue that general international law is relevant both to interpret the relevant treaty and to introduce doctrines not referred to in the treaty, including principles developed in treaties and case law outside the investment context, in particular international trade and human rights law—"extensive interpretation"; Pierre-Marie Dupuy, "Unification Rather than Fragmentation of International Law? The Case of International Investment Law and Human Rights Law" in Pierre-Marie Dupuy, Ernst-Ulrich Petersmann & Francesco Francioni, eds, *Human Rights in International Investment Law and Arbitration* (Oxford University Press, 2009) 45.

[406] Some commentators like Brower argue that investment tribunals should decide, to the extent possible, within the text of the governing treaty and the investment contract—"restrictive interpretation"; *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law: Report of the Study Group of the International Law Commission*, by Martti Koskenniemi (United Nations Publication, 2006) at 68.

In the next section, I will explore the pivotal role of Article 31(3)(c) of VCLT in shaping the interaction between rules of international law within ISDS tribunals. My focus will be on how judges and arbitrators across various institutions apply this article to reconcile the provisions of international treaties with external rules of international law.

2.3 Vienna Convention on the Law of the Treaties 1969

The VCLT, as a fundamental multilateral treaty that has 116 State parties[407] or its provisions in the capacity of reflecting customary international law,[408] serves as a mandatory reference point for treaty interpretation.[409] In particular, Article 31 of VCLT requires judges and arbitrators to interpret treaties "in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and light of its object and purpose."[410] Paragraph 3 of Article 31 then states that, together with the treaty's context, interpreters must also take into account:

> a) Any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions,
> b) Any subsequent practice in the application of the treaty that establishes the agreement of the parties regarding its interpretation, and
> c) Any *relevant rules* of international law *applicable* in the relations between the parties.[411]

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[407] "United Nations Treaty Collection", online: <https://treaties.un.org/pages/ViewDetailsIII.aspx?src=TREATY&mtdsg_no=XXIII-1&chapter=23&Temp=mtdsg3&clang=_en>.

[408] According to the International Law Commission, "The VCLT rules on treaty interpretation-article 31 and 32- are recognized as customary law"; *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law: Report of the Study Group of the International Law Commission*, by Martti Koskenniemi (United Nations Publication, 2006) at 89. For further discussion, see Anja Lindroos & Michael Mehling, "Dispelling the Chimera of 'Self-Contained Regimes': International Law and the WTO" (2005) 16:5 European Journal of International Law 857–877. For example, in *Noble Ventures, Inc v Romania,* ICSID Case No ARB/01/11, Award 12 October 2005, para 50*,* the tribunal stated:

> [R]eference has to be made to Arts. 31 *et seq*. of the Vienna Convention on the Law of Treaties which reflect the customary international law concerning treaty interpretation. Accordingly, treaties have to be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of the object and purpose of the Treaty, while recourse may be had to supplementary means of interpretation, including the preparatory work and the circumstances of its conclusion, only in order to confirm the meaning resulting from the application of the aforementioned methods of interpretation. Reference should also be made to the principle of effectiveness (*effet utile*), which, too plays an important role in interpreting treaties.

[409] Campbell McLachlan, "The Principle of Systemic Integration and Article 31(3)(C) of the Vienna Convention." (2005) 54 International Comparative Law Quarterly 279–320.

[410] note 4.

[411] *Ibid* Article 31(1) (emphasis added).

Section (c) of this paragraph, "any relevant rules of international law applicable in the relations between the parties," is of paramount importance for understanding the interaction between rules of international law, in ISDS tribunals. Textual analysis of Article 31(3)(c) emphasizes that treaty interpretation should be conducted with reference to rules of international law, under two major conditions: first, they must be "relevant" and second, they must be "applicable" in the relations between the parties.[412] Relevance means whether the rule of international law is related to the investment treaty being interpreted. Applicability means whether the rule of international law is both opposable between and legally binding on the disputing parties. Setting aside the second condition for now, which will be discussed thoroughly in Chapter 3, my primary focus here is on the first condition to recognize which rules of international law are "relevant" in the treaty interpretation process.

To arrive at the meaning of "relevant" and to operationalize Article 31(3)(c)—with the aim of understanding whether ISDS tribunals should interpret IIAs restrictively, in isolation from the broader international law, or extensively, with broad reference to the substantive content of other fields of international laws—I adopt the following two-step analysis. In the first step, I examine why treaty interpretation is not just necessary but pervasively required by understanding the changing nature of the international legal system that results in normative conflicts between rules of international law. In the second step, which constitutes the major argument of this chapter,

[412] Cases of outright conflict between rules of international law are likely to become more common in the future with proliferation of new rules and with later law tending to have different underlying concerns than earlier law. Given the growing prominence of issues of conflict, legal scholars criticize Article 31(3)(c) as inadequate because of the vagueness of its substantive scope in determining applicable international law. For example, the relationship between EU law and investment law raises many interesting issues and offers a microcosm of potentially conflicting international law obligations. The multiplicity of possibly inconsistent or conflicting obligations under the rules of international law needs legal practitioners to carefully determine *relevant* applicable laws. Yet, however limited the guidance of Article 31(1)(c) on the criteria for relevance, this does not make relevance analysis secondary let alone dispensable. To the extent that inadequate attention to relevant applicable laws, as stated by Carlston in the *BP Exploration Company (Libya) Limited v. Government of the Libyan Arab Republic* case, could invalidate final awards, "[a] decision which manifestly fails properly to apply a rule for decision laid down in the compromise or an applicable rule of international law involves an excess of jurisdiction and is therefore void." On this point, Judge Weeramantry noted, in the *Gabčikovo-Nagymaros* case, Article 31(3)(c) "scarcely covers this aspect with the degree of clarity requisite to so important a matter," *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*, *supra* note 3 para 1194. Likewise, Thirlway even doubts "whether this sub-paragraph [Article 31(3)(c)] will be of any assistance in the task of treaty interpretation," Hugh Thirlway, "The Law and Procedure of the International Court of Justice 1960–1989 (Part Three)" (1991) 62:1 British Yearbook of International Law at 58.

through case law analyses, I examine the legal reasoning of judges and arbitrators when they determine whether rules of international law are "relevant" in different dispute settlement scenarios. In other words, under what circumstances and in what ways do tribunals interpret treaties in light of external rules of international law? This analysis is foundational for understanding why and when transnational self-regulatory norms may now—or, in the future, could—be treated as applicable substantive law by ISDS tribunals in governing the outcome of investment disputes.

2.3.1 Changing Nature of the International Legal System

Regarding the changing nature of the international legal system, as one aspect of globalization, Higgins notes that international law is better understood as a normative system and a process rather than as a set of rules.[413] As globalization brings diverse actors—States, international organizations, corporations, and civil society—into closer interaction, she states that the normative framework of international law serves as a guiding structure for addressing common challenges rather than a static collection of rules. She wisely argues that one consequence of this perspective is that "this entails harder work in identifying sources and applying norms, as nothing is mechanistic and context is always important."[414] This perspective characterizes international law through three main traits: first, all international legal acts, including the making of treaties, form part of a broader legal system; second, the content of international law changes and develops continuously; and third, international law lacks a single legislature to develop rules for a hierarchy of norms. By framing international law as a normative system and a process, Higgins captures its adaptability and capacity to respond to the dynamic and interconnected nature of the modern international order. This understanding underscores the law's role not merely as a set of prescriptive rules but as a living framework for resolving disputes, promoting cooperation, and achieving common goals. This perspective aligns with the reality that legal norms are often subject to interpretation and must balance competing interests in a globalized world.

[413] See Rosalyn Higgins, *Problems and Process: International Law and How We Use It* (Oxford: Oxford University Press, 1994).
[414] *Ibid* at 8.

With globalization and the increasing complexity of international interactions, we have been witnessing for a considerable number of years now the emergence of technically specialized networks of issues such as trade, investment, the environment, and human rights, which have transcended national boundaries and have identified unique challenges that are difficult to regulate through traditional international law. National laws seem insufficient owing to the transnational nature of these issues, while international law inadequately takes account of their specialized objectives and needs. Such networks seek to advance their rule systems, which tends to result in the development of new international law regimes. These regimes have their basis in multilateral and specialized treaties tailored to each network's needs and interests.[415] What once appeared to be governed by general international law—which is the foundation of the whole system of international law, with its development often relying on international custom—has become the field of operation for specialized regimes that are comprised one or more treaties for governing a specific subject matter.[416] As explained by Koskenniemi, "a number of closely integrated sets of rules of international law pertaining to particular subject-areas" have been developed and are combined of "specific primary rules (rules laying down particular rights and obligations) with specific secondary rules (rules about rule-creation and change, responsibility and dispute settlement) that claim autonomy from principles of general international law."[417]

Brierly, who wrote in the immediate aftermath of the establishment of the modern (post-1945) international legal system, observed that this new class of international law-making treaties had become a major body of international law legislation.[418] These treaties, as discussed by Jenks, "are tending to develop in several historical, functional and regional groups which are separate from each other and whose mutual relationships are in some respects analogous to those of

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[415] Koskenniemi, *supra* note 406 para 483.
[416] The notion of regime attaches to the subject matter and its specialized treatment, and not as such to the form of a treaty. That said, the kind of specification and clarity of rules that help make clear the specialized treatment of a subject almost always rely either entirely—or at least, primarily—on treaties. This does not mean that custom may not cover some aspects of a regime or evolve to fill in gaps in specialized treaty regimes.
[417] *Fragmentation of International Law: Topic(a): The function and scope of the lex specialis rule and the question of "self- contained regimes"*, by Martti Koskenniemi (International Law Commission Study Group on Fragmentation, 2004) at 1 online: <https://legal.un.org/ilc/sessions/55/pdfs/fragmentation_outline.pdf>.
[418] James Leslie Brierly, *The Law of Nations: An Introduction to the International Law of Peace* (Clarendon Press, 1963).

separate systems of municipal law."[419] Legal scholars have then called this phenomenon *fragmentation of international law,* and sociologists have called it *functional specification*: the increasing specialization of the interests of the parts of society that need their governing principles and legal institutions for technically specialized networks of issues.[420] Such fragmentation and functional specification lead to the creation of *self-contained regimes* in international law—or, at least, of regimes that the most involved participants will often present as self-contained.[421] The notion of self-contained regime has been invoked to "cover[] a very wide set of differently interrelated rule systems, and the degree to which general law is assumed to be affected varies extensively."[422] These regimes comprise a group of special rules concerned with a particular issue and have their own institutional procedures and administrative techniques that sit alongside claims of a special foundational or purposive orientation for the given regime.[423] Functionally specialized treaties, which is another way self-contained regimes are sometimes described, often "contain tailor-made rules on the legal consequences of breach… [and] provide innovative procedures of dispute settlement, surveillance, and reporting, leading to remedies that

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[419] Wilfred Jenks, "The Conflict of Law-Making Treaties" (1953) 30 British Yearbook of International Law 401 at 403.

[420] As explained by Jeutner "[i]nternational law is to an extent 'fragmented', in the sense that there are various more or less disparate substantive sovereigns and regimes that are continuously created and modified by a multiplicity of different legal actors. Although this fragmentation is by no means a 'modern phenomenon', recent decades have witnessed a notable extension of the material scope of international law. Likewise, the number of actors who are subject to, and shape, international law has increased significantly. This enlargement of international law's material and personal scope makes the occurrence of conflicts between norms originating from different international legal regimes and enacted by different legal actors much more likely," Valentin Jeutner, "The Definition of a Legal Dilemma" in *Irresolvable Norm Conflicts in International Law: The Concept of a Legal Dilemma* (Oxford University Press, 2017) 17 at 51.

[421] See Eckart Klein, *Self-Contained Regime* (Oxford University Press, 2006) Max Planck Encyclopedia of Public International Law that explains:

> in international law the term 'self-contained regime' has been used over the years in different contexts and with a different legal meaning... [A] regime could be considered to be self-contained, if it comprises not only rules that regulate a particular field or factual relations laying down the rights and duties of the actors within the regime (primary rules), but also a set of rules that provide for means and mechanisms to enforce compliance, to settle disputes…, to modify or amend the undertakings …, and to react to breaches (secondary rules), with the intention to replace and through this to exclude the application of general international law …, at least to a certain extent.

Also find the whole discussion on self-contained regime in Chapter 3.

[422] Koskenniemi, *supra* note 406 at 32.

[423] A rule may be general or special in regard to its subject matter or in regard to the number of actors whose behavior is regulated by it. If we define self-contained regime as "a union of rules laying down particular rights, duties and powers and rules having to do with the administration of such rules," self-contained regime is categorized into the first case, a specialized subject matter that is also sometimes discussed using the term *lex specialis*, Koskenniemi, *supra* note 417. *Lex specialis* can have several meanings, and, for the purposes of this dissertation and this chapter, using that term with respect to this one form of *lex specialis*—self-contained regimes—does not add any value. Thus, I will limit myself to the term self-contained regimes.

did not previously exist under general international law."[424] The idea of self-contained regime is also part of the effort of international lawyers to make normative sense of the division of international law into different subject matter fields or subsystems, such as trade law, human rights law, environmental law, European law, and indeed investment law—each identified with special legal principles, field-specific administrative institutions, and specialized networks of actors engaging relevant issues.[425]

These legal subsystems do not emerge accidentally; instead, they are forged by interested actors seeking to respond to new and particular requirements of the globalized society.[426] Such resulting specific legal subsystems reveal the differing preferences that actors in a globalized society have and articulates contrasting perspectives of different regimes between factual situations or the interests considered most relevant in particular problem areas. Moreover, in an effort to make these self-contained regimes more effective in achieving the purposes of the regime, they often include new types of treaty clauses or practices that may not be compatible with the law of some other specialized regimes or even with general international law (on the basis of the particular or more specific operating as a normative carve-out from the general).[427]

For instance, the emergence of environmental law is a response to growing concern over environmental protection issues; trade law develops as an instrument to regulate international economic relations; human rights law aims to protect the interests of individuals (including individuals as members of protected social groups); and investment law seeks to protect foreign investors and facilitates the flow of FDIs. To further explain this specification, I would say that international investment law and human rights law are perceived by some, if not many, scholars and practitioners as two specialized regimes of international law with no substantial overlap. Human rights law is in essence focused on significant harms to individual *human* beings. While

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[424] Bruno Simma & Dirk Pulkowski, "Of Planets and the Universe: Self-contained Regimes in International Law" (2006) 17:3 European Journal of International Law 483–529 at 484.

[425] Although this division/classification is argued to be merely "relative," it is still playing an integral role in determining "relevant" rules in treaty interpretation. See the controversial discussion in P Malanczuk, "Space law as a branch of international law" in Karel C Wellens & LANM Barnhoorn, eds, *Diversity in Secondary Rules and the Unity of International Law* (The Hague; Boston: M. Nijhoff Publishers, 1995) at 144.

[426] Stephen D Krasner, "Structural Causes and Regime Consequences: Regimes as Intervening Variables" (1982) 36:2 International Organization 185–205.

[427] Specificity as a lawful exception to the general nonetheless meets an absolute limit in the case of peremptory norms of general international law, Koskenniemi, *supra* note 406 at 68.

investors can be individuals, investment law deals almost entirely with investors not as natural persons but as legal persons, in most cases as private corporations, and limits its understanding of harm to economic harm in investment-relevant contexts. It can be seen that self-contained regimes come with special principles, forms of expertise, and purposes that are not identical to—and may be extremely different from—those of other specialized bodies of international law. Note that this account also reflects a mainstream understanding—notably from the investment-law legal community—of the relationship between corporate behaviour and human rights as being solely a question of whether corporations can hold (or, at least, have standing to invoke) some human rights—e.g., media corporations in the realm of freedom of expression and information—and whether certain rights are even human rights (e.g., commercial property rights) and, if so, whether only humans are the beneficiaries. It does not even ask the question: can corporations be the holders not of rights but of human rights obligations—and, if so, owed to whom for what kinds of conduct. We shall see that it is this that has evolved into the area of substantial overlap between the two fields.

However, fragmentation of international law "may challenge the coherence of the international legal system."[428] Although the emergence of self-contained regimes is assumed to be a "natural" development to reflect the diversity of interests in the global society, international law professionals, like Brownlie, have long noted that the development of functionally specialized treaties could lead to conflicting rules of international law, conflicting institutional practices, and conflicting international obligations.[429] Self-contained regimes can exacerbate fragmentation of international law and risk creating incoherence in international law by creating "silos" where specialized regimes prioritize their own objectives over broader international concerns.[430] As self-contained regimes develop independently, their rules may diverge further and further from harmony with other regimes, generating overlapping or conflicting obligations.[431] For example,

[428] Koskenniemi, *supra* note 417 at 1.
[429] Ian Brownlie, "The Rights of Peoples in Modern International Law" (1985) 9 Bulletin of the Australian Society of Legal Philosophy 104.
[430] Simma, "Universality of International Law from the Perspective of a Practitioner" (2009) 20:2 European Journal of International Law 265–297.
[431] See Joost Pauwelyn, *Conflict of Norms in Public International Law. How WTO Law Relates to Other Rules of International Law* (Cambridge: Cambridge University Press, 2003). This book discusses the overlap and potential conflicts between WTO obligations and other international law obligations, such as environmental agreements.

environmental protection obligations under climate agreements might clash with trade liberalization rules under WTO agreements.

This potential for conflict is due to the emergence of a number of closely integrated sets of rules of international law pertaining to particular subject-areas such as human rights, the environment, trade, international crimes, and so on. Such sets often combine specific primary rules (rules laying down particular rights and obligations) with specific secondary rules (rules about rule-creation and change, responsibility and dispute settlement) that claim autonomy from principles of general international law. This autonomy has sometimes led to conflicts between such specialised sets of rules and the general law as well as between different sets of specialised rules. As explained by Jeutner, the diverse and often divergent interests of different legal actors involved in shaping international law "contribute significantly to the risk that conflicts between legal norms of different specialized regimes will arise."[432] Hafner also notes that the widespread development of specialized lawmaking treaties would impair the homogenous nature of international law.[433] For instance, when it comes to dispute settlement in ISDS tribunals, a State (A) might have conflicting obligations in regard to two (or more) different States (B and C)—depending, for example, on whether it has a BIT with each and then on what each BIT requires—and the question arises which of the obligations should prevail.

However, fragmentation demands consideration and development of means to administer interactions between rules of international law.[434] Judges and arbitrators are required by the terms of Article 31(3)(c) of VCLT itself to apply *systemic interpretation*—albeit, as we shall discuss extensively, as conditioned and complicated by the notion of *relevance* of one set of rules to another set in order to mitigate the risks of incoherence and promote harmony among self-contained regimes. Before moving to the next section on how systemic interpretation is used in courts and tribunals, I would highlight the essence of my earlier discussion on the fragmentation of international law in order to explain my view on systemic interpretation—that seeks both to

[432] Jeutner, *supra* note 420 at 52.
[433] Gerhard Hafner, "Pros and Cons Ensuing from Fragmentation of International Law" (2004) 25 Michigan Journal of International Law 849.
[434] Dinah L Shelton, "International Law and 'Relative Normativity'" in Evans, ed, *International Law* (Oxford; New York: Oxford University Press, 2003) at 148.

avoid contradictions between rules from different areas of international law and to respect the intentions of the parties who have entered into specific international agreements. I acknowledge that many legal scholars working in the field of sustainable development tend to approach systemic interpretation by simply emphasizing the overlaps, interactions, and connections between different legal regimes, as well as by counterposing these systemic relations to an unacceptable (often termed "formalistic") view of them as isolated or "hermetically sealed" from one another. Within this approach—without detailed argumentation on the mechanisms of relevance and applicability that are integral subjects of this dissertation—scholars often encourage ISDS tribunals to interpret investment treaties in line with international environmental norms. This reflects an embrace of systemic interpretation as the prevailing approach to treaty interpretation and generally as well as aligning with the ILC's treatment of self-contained regimes.

However, I take a different view, one which embraces systemic interpretation by rejecting watertight-compartment characterizations of different fields but also one that does not see a general call for "systemic" interpretation as a panacea. My view is one of specialization first, generalization second: it helps explain and accommodate why international law consists of different specialized subjects and then argues the paths of interaction between these self-contained regimes. Bolstered by the sociological observation that there *is* functional specialization amongst international law professional sub-communities, the current practice of ISDS tribunals, the ICSID Travaux, and the subject-matter detail and targeted primary purpose (protecting investors' rights against arbitrary state conduct) of investment treaties, I take the view that the simplified systemic integration model under the International Law Commission's treatment of self-contained regimes is not fully adequate for the interpretation of investment treaties in ISDS tribunals.

Unlike the broader understanding of systemic interpretation, my approach seeks to integrate the realities underlying a fragmentation theory of international law. This perspective recognizes investment law as a distinct, specialized regime with its own normative boundaries. Yet, it simultaneously seeks a balanced and nuanced opening of investment treaties to incorporate considerations of foreign investors' environmental (and other) responsibilities—without

undermining the fundamental protective rights these treaties grant investors vis-à-vis host States. In short, while systemic interpretation rightly highlights the interconnectedness of international law, the unique character and function of investment treaties demand a more contained, specialized interpretive approach, one that carefully negotiates the interface between investor protections and sustainable development concerns. My view—one that neither assumes all rules of environmental law are inherently relevant and applicable in treaty interpretation, nor categorically excludes the relevance and applicability of these and other rules of international law—offers, I believe, a more balanced approach to systemic interpretation. Given my very case-specific approach towards systemic interpretation, in the next sections, I will explain a nuanced framework for reconciling the competing priorities of investment protection and environmental considerations, without compromising the functional specialization of investment law—all the while embracing systemic interpretation to the greatest extent normatively justifiable.

2.3.2 Legal Reasoning and Interpretive Approaches

The issue of fragmentation within the international legal order should be discussed with reference to Article 31(3)(c) of VCLT, which suggests *systemic interpretation* for the sake of "promoting harmonization and guaranteeing the unity of the international legal system" in order to reduce fragmentation within the legal order.[435] Article 31(3)(c) emphasizes the unity of international law in that treaty rules should not be considered as fragmented from general international law. Systemic interpretation should be then applied to uphold that special treaties are creatures of international law and consider a dialectic between the treaty text itself and the legal system from which it draws breath to reduce conflicts between rules of international law.[436] In this approach, special treaties must be "applied and interpreted against the background of the general principles of international law."[437] Under systemic interpretation, treaties are not self-contained regime to be fragmented instruments but derive their binding force and legitimacy from the overarching

[435] As McLachlan notes, "[i]t is no accident that this renewed attention [on Article 31(3)(c)] has surfaced at a time of increasing concern about the fragmentation of international law—a concern that the proliferation of particular treaty regimes would not merely lead to narrow specialization, but to outright conflict between international norms," McLachlan, *supra* note 409 at 280.
[436] See Panos Merkouris, *Article 31(3)(c) VCLT and the Principle of Systemic Integration: Normative Shadows in Plato's Cave* (Brill Nijhoff, 2015).
[437] Lord McNair, *The Law of Treaties* (Oxford, New York: Oxford University Press, 1961) at 466.

framework of international law and set up rights and obligations that exist alongside rights and obligations established by other rules of international law.[438]

To understand how judges and arbitrators apply Article 31(3)(c) in judicial practice to administer interactions, I focus on the first parameter of being *relevant* and also consciously narrow the scope of my analysis to the interpretation of treaties only by reference to customary international law. Confining this analysis to interactions between treaties and customary international law—without considering how a treaty could interact with another treaty or how two provisions within a treaty would interact—[439] aligns with my research objective to understand whether transnationalized customary international law could be treated by ISDS tribunals as substantive law in the investment disputes settlement procedures.

To do so, I ground my research in the International Law Commission's seminal framework as articulated in *Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law.* Given its role as the body that originally prepared VCLT, the International Law Commission is uniquely positioned to analyze and address the complexities and challenges associated with the fragmentation of international law. I also draw on secondary legal scholarship and detailed case law analyses to examine how courts in practice interpret the term "relevant" rule of international law under Article 31(3)(c) of the VCLT. Additionally, I analyze the predominant approaches courts adopt to resolve conflicts between treaty provisions and customary international law, highlighting the practical methodologies employed in such scenarios.[440]

To set the context for my case law analyses, I must clarify two foundational points that define the domain and scope of my inquiry. First, the interpretive approaches employed by ISDS tribunals in resolving conflicts between rules of international law have frequently evolved through reliance

[438] Odile Ammann, "The Interpretative Methods of International Law: What Are They, and Why Use Them?" in *Domestic Courts and the Interpretation of International Law* (Brill Nijhoff, 2020) 191.
[439] To know about the l*ex posterior* and the *lex superior* techniques for conflict resolution, see Erich Vranes, *"*The Principles of Conflict Resolution*"* in *Trade and the Environment: Fundamental Issues in International Law, WTO Law, and Legal Theory* (Oxford Scholarship Online, 2009) 39.
[440] Questions on which norms would be considered as rule of international law *applicable* in the relations between the parties will be examine in Chapter 3.

on the jurisprudence of other prominent international judicial bodies, notably the International Court of Justice (ICJ) and the organs of the World Trade Organization (WTO).[441] Accordingly, to comprehensively illustrate the treaty interpretation techniques available to ISDS tribunals for addressing such conflicts, I expand my analyses to include cases from a range of non-ISDS fora, including the Iran-United States Claims Tribunal, the European Court of Human Rights (ECtHR), and the WTO Appellate Body. This broader scope highlights cross-institutional influences and comparative practices in treaty interpretation. Second, my selection of case law is guided by specific principles to ensure that the analyses presented are both representative and appropriate to the interpretive challenges faced by ISDS tribunals. These principles include the relevance of the cases in shaping interpretive methodologies for managing interactions between treaty rules and customary international law and their significance in reflecting widely recognized principles in the practice of treaty interpretation under Article 31(3)(c) of VCLT:

- Focus: I select cases that are directly relevant to the legal issue of treaty interpretation by referring to customary international law. Although conflicts between a treaty and rules of international law could be categorized in different clusters, I bracket conflicts between the provisions of a treaty, conflicts between two non-treaty sources of international law, and conflicts between two treaties. I focus only on analyzing the interpretive approaches of courts when there are differences and conflicts between a treaty and customary international law regardless of its source.[442]
- Significance: through a comprehensive literature review, I have identified and selected significant or leading cases that have played a pivotal role in shaping the law on treaty interpretation. These cases are distinguished not only by their substantive contributions

[441] Zaneta Sedilekova & Josh Dries, "Conflict of Norms in International Arbitration – Friend or Foe in the Fight against Climate Change?" (2 November 2021), online: <https://blog.jusmundi.com/conflict-of-norms-in-international-arbitration-friend-or-foe-in-the-fight-against-climate-change/>.

[442] Although, there is no well-articulated or uniform understanding of what this might mean, general international law often refers to general customary law, as well as to the general principles of law under Article 38(1)(c) of the Statute of the International Court of Justice. There is no generally established distinction between customary international law and the general principles of law. The distinction will be based on how tribunals have classified the norms in question. However, there are examples where one tribunal has characterized a norm as customary international law while another tribunal has characterized the same or a very similar norm as a general principle of law. In this research, then, these two terms are used interchangeably within the wider category of (non-treaty) general international law.

but also by their influence, as evidenced by their adoption or citation in subsequent decisions by other courts and tribunals.

This case law analyses offers pragmatic frameworks for treaty interpretation in light of customary international law even as, nonetheless, a case-by-case approach will still be necessary for IIA interpretation. It enables me to highlight trends and problems when ISDS tribunals come to determining whether transnational self-regulatory norms, if and when they were recognized as transnationalized customary international law, are "relevant" rules of international law for interpreting investment treaties. However, any generalization of trade law disputes or human rights disputes (to take the two fields from which much of the case law arises) to interpret investment treaties and the interaction among IIAs and customary environmental law in ISDS tribunals must be approached with caution. Each legal field has unique objectives, contexts, and normative frameworks that may not seamlessly translate into investment law. As such, this analysis is not intended to offer a rigid template but rather a flexible toolbox to help lawyers and arbitrators in navigating the complexities of using transnational self-regulated norms or analogous normative sources in the investment dispute settlement procedures, ultimately supporting reasoned and well-grounded decision-making processes.

2.4 Relations among Treaty Law and Customary International Law

The special nature of treaties requires courts to adequately administer interactions among them and other sources of international law based on systemic interpretation to ensure that treaty law is applied consistently and harmoniously with the relevant rules of international law, preserving both the autonomy of the specific regime and the coherence of the legal system as a whole.

Such interpretation enables a systemic relationship between different rules of international law by guiding the selection of "relevant" rules in a way that aligns with the perceived purposes and objectives of the broader international legal system.[443] To know how courts apply systemic interpretation for determining "relevant" rules of customary international law in treaty interpretation, under Article 31(3)(c) of VCLT, there are two consequential criteria:

[443] W Czapliński & G Danilenko, "Conflicts of Norms in International Law" (1990) 21 Netherlands Yearbook of International Law 3–42.

A) sameness of the subject matter of treaty law and customary international law, and
B) consistency among rules of treaty law and customary international law.

Briefly explaining, the first step for determining "relevant" customary international law in the treaty interpretation process is to correctly identify whether both treaty law and customary law correspond with *the same subject matter*.[444] On the contrary, when treaty law and customary international law concern different subject matters, it is suggested that systemic interpretation will be removed and that correspondingly there is no room for harmonizing the two rules because of the non-correspondence of the subject matter. Here, having different subject matters makes recourse to systemic interpretation futile in administering interactions between the two rules.[445] A major caveat is in order here, though: much depends on the characterization exercises (are we dealing with the same subject matter or not) and, if an unstated tendency of characterizing specialized treaty subject matter as different from invoked custom in order to avoid the need to harmonize develops, then getting rid of the need to harmonize may simply be the result of arbitral panels acting with a loyalty bias to the treaty regime and a corresponding narrow view of the subject matter (economic investment being treated not as in the same field as environmental protection for sustainable development). This is to say that characterization—what is and what is not the same subject matter—is neither obvious nor neutral, and is instead the outcome of human interpretive activity by actors who may come at the question from very different starting points.

Here we need a test of norm-by-norm actual conflict of obligations instead of examining consistency between two bodies of law. And one branch of the principle of *lex specialis*— in the sense of a specific group of States consenting to set aside general norms—requires that the reciprocal interests of the parties must be achieved by applying the special norm.

[444] Because only those that are in some respect similar can be compared—and indeed can enter into conflict—it must be assumed, together with Fitzmaurice, that *lex specialis* "can only apply where both the specific and general provisions concerned deal with the same substantive matter," Gerald Fitzmaurice, "The Law and Procedure of the International Court of Justice 1951-4: Treaty Interpretation and Other Treaty Points" (1957) 33 British Yearbook of International Law 203 at 237.
[445] See Rhonda Ferguson, "Conflict of Norms in International Law: Theories and Practice" in *The Right to Food and the World Trade Organization's Rules on Agriculture* (Brill | Nijhoff, 2018) 51.

In the second step, once the sameness of subject matter is ascertained, consistency between rules of treaty law and customary law should be determined.[446] Consistency is a legal idea that refers to the absence of actual conflict (an actor can comply with both sets of obligations). If treaty law and customary law are consistent (where a treaty is deemed to be a reflection, declaration, or codification of customary law and/or customary law is offering contextual background for treaty interpretation by shaping the broader legal landscape in which the treaty's provisions operate) both laws are systemically applied for the treaty interpretation.[447] This consistent nexus suggests that treaties and customary international law operate as complementary components that are needed to be harmonized through systemic interpretation where customary international law—notably, as it evolves—informs the interpretation of treaty provisions ensuring coherence within the broader legal order. However, treaties can create *inter se* exceptions for or modifications to the existing rules of customary international law, excluding *jus cogens*, by deviating from certain requirements/obligations established by customary international law. In such instances, under consent-based exceptions, a smaller group of actors carve out from generally applicable norms of custom with the result that treaty law and customary law point in conflicting directions for dealing with those requirements/obligations (an actor being forced to violate one obligation in order to comply with another). In such cases, *lex specialis* serves as a rule of priority, allowing the specific treaty norm to replace/override the general customary rule—but only as far as the conflict goes.[448]

These two integral criteria of the *same subject matter* and *consistency* guide the application of Article 31(3)(c) of the VCLT. By the means of systemic interpretation, harmonization among rules of international develops towards a careful and balanced approach in order to "avoid unjustifiably including the same rules of international customary law that the contracting states sought to avoid by making a treaty."[449]

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[446] The question then is whether those provisions are exclusive, i.e. whether the consequences which would otherwise apply under general international law, or the rules that might otherwise have applied for determining a breach, are thereby excluded, Koskenniemi, *supra* note 406 at 50.
[447] Christopher J Borgen, "Resolving Treaty Conflicts" (2005) 37 George Washington International Law Review 573 at 603.
[448] Koskenniemi, *supra* note 406.
[449] Jeswald W Salacuse, "The Interpretation of Investment Treaties" in *The Law of Investment Treaties*, 3rd edn (Oxford Scholarly Authorities on International Law [OSAIL], 2021) 184 at 196.

2.4.1 The Sameness of the Subject Matter

The concept of *sameness of subject matter* serves as a key criterion for identifying the "relevant" rule of customary international law during the systemic interpretation of treaty law.[450] However, the scope of what constitutes sameness can be viewed from various perspectives, each of which influences the extent to which the term relevant is interpreted, either broadly or narrowly, in practice. These differing perspectives arise from divergent interpretations of how closely a customary rule must align with the treaty's subject matter to be considered relevant. This variability underscores the importance of adopting a moderate approach, one that balances flexibility with precision, in order to ensure a coherent and context-sensitive application of systemic interpretation. Below is an explanation of the different perspectives and why a moderate approach is essential for the purposes of this study, as it facilitates a nuanced and practical understanding of how customary international law and treaty law interact in complex legal frameworks.

At the narrower end of the spectrum, Judge Villiger has suggested that relevant rules "concern the subject matter of the treaty term at issue. In the case of customary rules, these may even be identical with, and run parallel to, the treaty rule."[451] In this approach, general international law is assumed to not be relevant at all for treaty interpretation if two bodies of law do not correspond with respect to the subject matter (or have sufficient subject matter overlap). The importance of the sameness (or sufficiently similarity) of the subject matter in determining the relation between rules of international law is pointed out by Waldock, who notes that if the treaty was intended to create a special regime between the particular parties, they might not intend it to be displaced by general rules of international law that are not dealing with similar subject matter.[452] The cruciality of the same subject matter in resolving normative conflict is also emphasized by Kelsen: "The work of interpretation is one of discovering the intention of the parties not only by reference to rules of interpretation but to rules of international law bearing upon the subject matter of the

[450] International Law Commission (ILC), *supra* note 214.
[451] Mark Eugen Villigeer, *Commentary on the 1969 Vienna Convention on the Law of Treaties* (Leiden/Boston: Martinus Nijhoff Publishers, 2009) at 433.
[452] Humphrey Waldock, "Third Report on the Law of Treaties" in *Yearbook of the International Law Commission Volume II* (United Nations, 1964).

disputed contractual stipulation."[453] Likewise, the commentary to Article 55 of the Draft Articles on Responsibility of States for Internationally Wrongful Acts requires that for "systemic interpretation" to apply, the rules must deal with the "same subject matter." It is due to an argument that an obligation dealing with a certain subject matter could conflict only with the conduct of the same subject, as a result of which systemic interpretation should be applied to manage such conflict.[454] Systemic interpretation, in Fitzmaurice's reasonings, also "can only apply where both the specific and general provisions concerned deal with the same substantive matter."[455]

At the other end of the spectrum, Judge Simma and Theodore Kill have argued for a broad reading under which "almost any rule of international law will be 'relevant' when considered with the proper degree of abstraction."[456] They challenge the usefulness of the criterion of subject-matter sameness for determining the relevant rules of customary international law in treaty interpretation by asking whether the criterion of the same subject matter can define the scope of systemic interpretation in normative conflicts, as the above discussion and associated scholars assume. Instead, they argue that systemic interpretation should allow for consideration of rules from diverse legal domains, ensuring consistency and coherence in international law. In cases of normative conflict, where different legal obligations intersect (e.g., human rights law and trade law, or environmental law and investment law), rigid adherence to subject matter sameness may hinder holistic interpretation. Their argument implies that legal interpretation should consider broader legal frameworks, even if the rules do not strictly pertain to the same subject matter. A broader interpretation allows for cross-referencing between different legal regimes, promoting a more dynamic and evolving understanding of international law. Their view is particularly useful in addressing complex legal disputes where multiple legal regimes interact (e.g., international investment disputes involving human rights concerns).

Correspondingly, scholars such as Brownlie and Pellet have been quite critical of what they see as excessive emphasis on the cruciality of the same subject matter for applying customary

[453] Hans Kelsen, *Pure Theory of Law* (Berkeley: University of California Press, 1970) at 355.
[454] International Law Commission (ILC), *supra* note 214 at 140.
[455] Fitzmaurice, "The Law and Procedure of the International Court of Justice 1951-4", *supra* note 444 at 237.
[456] Simma & Kill, *supra* note 405 at 696.

international law external to the special treaty.[457] They argue that the criterion of the same subject matter does not map one to one onto the nature of a treaty, which is supposed to be understood through systemic interpretation. Instead, the nature of a treaty is "relative" and, in practice, links to the "interest" of and associated perspective from which the observer assesses the treaty. For example, the treaty on the maritime transport of chemicals relates at least to the law of the sea, environmental law, trade law, and the law of maritime transport. The treaty may be characterized differently depending on what regulatory purpose one has in mind, and the characterizations have less to do with the "nature" of the instrument than the interested perspective from which it is described. Since in assessing the sameness of subject matter, the focus depends both on the object that is being regulated and on an abstract characterization of an issue as a "human rights issue," an "environmental problem," or a "trade question," we cannot avoid the challenge created by the fact that different actors may have the interest to characterize a single problem in different ways so as ensure that their preferred rule-systems will be applied.

Despite these polarized approaches, a growing moderate position emerges—aligned with my view of systemic interpretation that confirms international law consists of different specialized subjects while still requiring integration of general international law rules (e.g. those on state responsibility and on the law of treaties) and also while allowing and indeed actively encouraging paths of interaction between (so-called) self-contained regimes. This approach provides a comprehensive framework for assessing the (so-called) sameness of the subject matter of transnational self-regulated norms in comparison to investment treaties. This approach contends that, under Article 31(3)(c) of VCLT, tribunals must remain committed to making the effort to consider the treaty's subject matter and engage "rules of customary international law *affecting* the subject matter of the treaty" even if the subject matter of the treaties and the rules may not be easily characterizable as the same.[458]

This is a middle position between a conceptually and linguistically narrow focus on subject-matter labels, on the one hand, and broad assertions that ultimately all custom is relevant to all

[457] Brownlie, *supra* note 429.
[458] Waldock, *supra* note 162 at 53 (emphasis added).

treaties because everything must be understood to cohere and systemically hold together. The moderate approach strikes a balance by including rules that have a clear and demonstrable connection to the treaty in question, while ensuring those rules align with both the object and purpose of the particular treaty and the broader framework of international law. In the moderate approach, sameness of subject matter should be assessed in accordance with: 1) object and purpose, 2) context and topic, 3) value compatibility.

Scholars following one version or another of such a moderate perspective argue object and purpose, which illuminate the normative goals and functional roles each rule is intended to serve, are integral factors in assessing the sameness of two rules of international law.[459] The object of a treaty is "the instrument for the achievement of the treaty's purpose, and this purpose is, in turn, the general result which the [P]arties want to achieve by the treaty."[460] The moderate functional approach, which goes beyond a semantic matter, emphasizes the role of both the substantive purposes and the conduct-shaping object (and associated mechanisms) of treaty law—in general and in relation to a specific treaty—in determining relevant rules of customary international law.[461] In this context, Sands argues that "norms arising in different subject-matter areas can and do touch" if, given their different overarching terms ("investment" versus "environment"), they either be essentially the same in purpose (as in 'regulation of lawful taking of life' when "international human rights law" is contrasted to "international humanitarian law") or sufficiently integrated that they cannot be disentangled in areas of overlap (as in, environmentally-impactful investment decision and investment-impactful environmental regulation).[462] He also notes that the language of Article 31(3)(c) establishes a number of parameters among which in order to take customary norms into account in interpreting a treaty, "it must be 'relevant'… [and] '[r]elevance' refers to the subject matter—it should be related in some way to the treaty norm being interpreted."[463] He then points out the importance of "object and purpose" in assessing whether

[459] Philippe Sands, "Sustainable Development: Treaty, Custom, and the Cross-Fertilization of International Law" in Alan Boyle & David Freestone, eds, *International Law and Sustainable Development: Past Achievements and Future Challenges* (Oxford University Press, 1999); Cordonier Segger, *supra* note 7.
[460] Richard K Gardiner, *Treaty interpretation*, second edition ed (Oxford, United Kingdom; New York, NY: Oxford University Press, 2015) at 213.
[461] Martti Koskenniemi & Päivi Leino, "Fragmentation of International Law. Postmodern Anxieties?" (2005) 15 Leiden Journal of International Law.
[462] Sands, *supra* note 459 at 43.
[463] *Ibid* at 57.

the treaty and general international law deal with the "same subject matter" by recalling Article 31(1) of VCLT that a treaty is to be interpreted "in good faith in accordance with the ordinary meaning to be given to [its] terms…in their context and in the light of its object and purpose."[464] Sands explains this approach in the relationship between the Basel Convection and WTO treaties, by saying that "the WTO system (indeed the rules of any primarily self-contained system of rules) is to be interpreted consistently with general international law, and that the customary rule is to apply, unless it can be shown that such application would undermine the object and purpose of the WTO system."[465]

To further elaborate on the functional approach, instead of approving the broad assertion of the court with regard to the relevance of external rules of international law, Higgins takes a moderate approach and highlights the importance of "the context" and "topic" in assessing the sameness of the subject matter of customary international law and treaty law. Higgins' argument as an International Court of Justice judge in the *Oil Platforms* case underscores the critical role of context in determining whether customary international law and treaty law share the same subject matter, thereby influencing the relevance of customary rules in treaty interpretation.[466] She critiqued the ICJ's broad approach to incorporating customary international law into treaty interpretation and then interpreted a provision of the treaty in light of broad principles of international law on the use of force under Article 31(3)(c) of the VCLT, which mandates that relevant rules of international law be taken into account in interpreting a treaty. Her main point was that context matters in defining "relevant" rules. While the ICJ read Article 31(3)(c) as incorporating the entirety of substantive international law—including Charter law on the use of force—Higgins argued that this approach is overly expansive and disregards the treaty's specific context.[467] She explained that "[t]he Court reads this provision [Article XX, paragraph 1(d) of 955 Treaty of Amity, Economic Relations, and Consular Rights] as incorporating the totality of the substantive international law (which in paragraph 42 of the Judgment is defined as

[464] Article 31(1) of VCLT states "treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."
[465] Sands, *supra* note 459 at 58.
[466] Article 31(3)(c) of VCLT states that, in interpreting a treaty, "There shall be taken into account, together with the context, … any relevant rules of international law applicable in the relations between the parties."
[467] separate opinion of Judge Higgins, para 45.

comprising Charter law) on the use of force."[468] Higgins criticized the court's decision and says one should not "ignore that Article 31, paragraph 3 [of the VCLT], requires "the context" to be taken into account: and "the context" is that of an economic and commercial treaty."[469]

The treaty in question was an economic and commercial agreement between Iran and the United States, and Higgins emphasized that this should have guided the court's determination of which rules of international law were relevant. Instead of broadly incorporating the general principles of the use of force, the interpretation should have been constrained by the treaty's economic subject matter and the specific legal framework governing Iran-U.S. relations. She further stressed the importance of "topic" in identifying relevant rules, arguing that only rules connected to the treaty's subject matter should be considered. She noted that "[w]hat is envisaged by Article 31, paragraph 3 (c), is that a provision that requires interpretation in Article XX, paragraph 1 (d), will be illuminated by recalling what type of a treaty this is and any other 'relevant rules' governing Iran-United States relations. It is not a provision that on the face of it envisages incorporating the entire substance of international law on a topic not mentioned in the clause—at least not without more explanation than the Court provides."[470] The court's failure, in her view, was in assuming that any general rule of international law—such as the use of force—was automatically relevant to interpreting a treaty that was not primarily concerned with that issue. Higgins' critique in *Oil Platforms* argues that systemic interpretation must be applied contextually, ensuring that the integration of customary international law aligns with the treaty's functional purpose and legal scope**.**

In this perspective, even if legal norms originate from different areas, they may reflect or foster compatible values. They can thus still be considered part of the same subject matter as they serve similar regulatory concerns or are coherent enough that they cannot be separated. Value compatibility therefore is also of paramount importance in determining sameness of subject matter as it refers to the idea that both legal regimes, treaty law and customary international law, reflect or promote compatible underlying values. Suppose an investment treaty promotes non-

[468] *Ibid* separate opinion of Judge Higgins, para 46. Text of Article XX(1)(d): The present Treaty shall not preclude the application of measures [...] necessary to protect essential security interests.
[469] *Ibid* separate opinion of Judge Higgins, para 46.
[470] *Ibid* separate opinion of Judge Higgins, para 46.

discriminatory treatment of parties and customary international law also mandates due process. Even if they arise in different subject matter domains (investment law vs. human rights law), if they both protect against unfair treatment, they might be seen as expressing a compatible value—thereby supporting integration or mutual reinforcement.

I believe that the moderate approach to determining the sameness of treaty law and CIL offers the appropriate framework for assessing the relevance of transnational self-regulated norms in treaty interpretation. This approach strikes a necessary balance between two competing impulses in international legal reasoning. It respects the fragmentation of international law by acknowledging that different legal regimes—such as investment law and environmental law—have developed distinct institutional structures, sources, and normative priorities. At the same time, it recognizes the systemic nexus among rules of international law that increasingly characterizes contemporary international legal problems, especially where multiple regimes interact around common regulatory concerns like sustainable development or corporate accountability. This moderate position justifies the characterisations required for the examination of how transnational self-regulated norms imposing environmental obligations on foreign investors could be relevant to investment treaties dealing with States' obligations towards investors' protection. It provides a disciplined and legally grounded method for evaluating when and how these norms can play a role in interpreting treaty obligations.

2.4.1.1 Case Law

The case law analysis on the arbitral proceeding of *Bernhard von Pezold and others v. Republic of Zimbabwe (2015)* is an example that shows the moderate position towards using Article 31(3)(c) of VCLT in the treaty interpretation process.[471] In this case, instead of saying that all rules of international law are relevant or nothing beyond the investment treaty is relevant, the tribunal conditioned an assessment of the relevance of the United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP) on the sameness of its subject matter with investment treaty. In this case, the tribunal considered the UNDRIP as a rule of international law external to the treaty text, as "relevant" only if one or more of its provisions were closely aligned with the

[471] *Bernhard von Pezold and others v. Republic of Zimbabwe,* ICSID Case No ARB/10/15, Award 28 July 2015.

treaty's subject matter *and* addressed an issue within the scope of the dispute.[472] This means that the applicability of the external legal rule depended on its connection to the treaty's core purpose and the specific legal questions at hand in the dispute. However, because there was no evidence demonstrating the importance of the UNDRIP to the applicable BIT, the tribunal rejected the application of the rule and dismissed an *amicus curiae*'s petition to participate in the hearings.

Bernhard von Pezold and others v. Republic of Zimbabwe

This dispute arose under the Germany-Zimbabwe Bilateral Investment Treaty after the Zimbabwean government expropriated land owned by the claimants, who were foreign investors and German Nationals. The claimants alleged breaches of treaty obligations, including expropriation without compensation and failure to accord fair and equitable treatment. Zimbabwe argued that its actions were justified based on its regulatory power to address historical injustices, including land redistribution for the benefit of the local indigenous population, which it framed as a human rights imperative. Against this background, on 23 May 2012, the European Center for Constitutional and Human Rights ("ECCHR") and four Indigenous communities of Zimbabwe (the "Indigenous communities") filed a Petition to make submissions as an *amicus curiae* to attend the hearings in the conjoined arbitral proceedings of *Bernhard von Pezold and others v. Republic of Zimbabwe.* They submitted that article 26 of the UNDRIP should be involved as relevant rule of international law in interpreting the investment treaty. Article 26 reads:

[472] I initially discussed the *Pezold* case to illustrate how ISDS tribunals approach the "sameness of subject matter" when determining the relevance of international legal rules external to the treaty, here the UNDRIP. However, in light of the very observant remarks of Professor Neil Craik (on an earlier draft of this chapter) on the ISDS tribunal's approach to the normative force of the UNDRIP despite its formally non-binding nature as an UN General Assembly resolution, I can see now the *Pezold* case serves as a well-articulated example for my discussion in Chapter 3 on the normative force of transnational norms that fall outside the traditional sources of international law. I now realize that the UNDRIP is one of the best possible examples of transnational norms that are generated by the ongoing involvement of multiple actors well beyond only States in the interactional normative process. Professor Scott also has indicated that this paradigm for thinking about the UNDRIP was clear at least 30 years ago already, for example when he wrote a 1992 conference paper in which he discusses the normative dimensions of the UNDRIP (even when still a draft) in terms of transnational interactive norm creation and normative rules that exist in a transnationalized space versus a traditional public international law space, Craig M Scott, "Dialogical Sovereignty: Preliminary Metaphorical Musings" (1992) 21 Proceedings of the Canadian Council on International Law 267–293.

1. Indigenous peoples have the right to the lands, territories, and resources which they have traditionally owned, occupied, or otherwise used or acquired.
2. Indigenous peoples have the right to own, use, develop, and control the lands, territories, and resources that they possess by reason of traditional ownership or other traditional occupation or use, as well as those they have otherwise acquired.
3. States shall give legal recognition and protection to these lands, territories, and resources. Such recognition shall be conducted with due respect to the customs, traditions, and land tenure systems of the indigenous peoples concerned.[473]

The Petitioners stated that its significant interest in the arbitration proceedings is determined by its mission to develop the strategic use of legal actions for corporate human rights responsibilities. They note that regional and international human rights institutions, including the United Nations and the Inter-American Court of Human Rights, have identified the relationship between investment treaties and indigenous peoples' rights as critical to the effect of human rights protection, and thus the application of BITs should be in compliance with international human rights law.

In this regard, the Petitioners contended that in light of the "interdependence of international investment law and international human rights law," any decision in these conjoined arbitrations which neglects the content of the international human rights norms will be "legally incomplete."[474] Accordingly, they urged the tribunals to give due consideration to the duties of States and the responsibilities of companies with respect to the rights of indigenous communities—and thus to permit their involvement as amicus. The Petitioners submitted that Article 26 of the UNDRIP must be applied to these arbitrations in parallel to the relevant BITs and the ICSID Convention:

> Article 42(1) of the ICSID Convention provides that the 'Tribunal shall decide a dispute in accordance with such rules of law as may be agreed upon by the parties', and that 'in the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws), and such rules of international law as may be applicable.' Under the BITs entered into by the Republic of Zimbabwe with the Federal Republic of Germany and with the Swiss Federation respectively, the tribunal is mandated to reach its decisions on the basis of the BITs themselves, any treaties in force between the Contracting Parties, such rules

[473] United Nations, *United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP)* (2007), online: <https://docs.un.org/en/A/res/61/295>.
[474] *Bernhard von Pezold and others v. Republic of Zimbabwe,* ICSID Case No ARB/10/15, Procedural Order No 2, 26 Jun 2012, para 26.

of general international law as may be applicable, and the domestic law of the Contracting Party in the territory of which the investment in question is situated.[475]

In its analysis, the tribunal allowed the Petitioners to make a submission based on Article 26 of the UNDRIP if their submission was aligned with Rule 37(2) of the BIT. This Rule states:

a) the non-disputing party submission would assist the Tribunal in the determination of a factual or legal issue related to the proceeding by bringing a perspective, particular knowledge or insight that is different from that of the disputing parties;
b) the non-disputing party submission would address a matter within the scope of the dispute;
c) the non-disputing party has a significant interest in the proceeding.[476]

However, the tribunal was not persuaded that the Petitioners should be permitted to make a submission in these proceedings: "having considered the Application in light of all of the criteria set out in Rule 37(2), the Arbitral Tribunals are not persuaded that the Petitioners should be permitted to make a submission in these proceedings because they have not satisfied any of the criteria in Rule 37(2)."[477] This followed from the tribunal's two major lines of reasoning regarding the sameness of the treaty's subject matter with that of Article 26 of the UNDRIP.

First, the tribunal held that: "The Petitioners do not propose to make submissions that would assist them 'in the determination of a factual or legal issue related to the proceeding', as is required by Rule 37(2)(a). The Petitioners, in effect, seek to make a submission on legal and factual issues that are unrelated to the matters before the Arbitral Tribunals. The Arbitral Tribunals agree in this regard with the Claimants that the reference to 'such rules of general international law as may be applicable' in the BITs does not incorporate the universe of international law into the BITs or into disputes arising under the BITs. Moreover, neither Party has put the identity and/or treatment of indigenous peoples, or the indigenous communities in

[475] *Ibid* para 25.
[476] *Agreement between the Republic of Zimbabwe and the Federal Republic of Germany Concerning the Encouragement and Reciprocal Protection of Investment* (1995), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/1453/download> Rule 37(2).
[477] *Bernhard von Pezold and others v. Republic of Zimbabwe,* ICSID Case No. ARB/10/15, Procedural Order No. 2, 26 June 2012, *supra* note 474 para 56.

particular, under international law, including international human rights law on indigenous peoples, in issue in these proceedings."[478]

Second, the tribunal noted that the Petitioners' submission did not address a matter within the scope of the dispute. It said that "the disputes in these conjoined arbitrations arise out of the allegedly unlawful measures taken by the Respondent against the Claimants and their investments pursuant to the LRP [Land Reform Programme]. As noted above, the Petitioners propose to make a submission on the putative rights of the indigenous communities as 'indigenous peoples' under international human rights law, a matter outside of the scope of the dispute, as it is presently constituted. Indeed, as the Claimants have noted, in order for the Arbitral Tribunals to consider such a submission, they would need to consider and decide whether the indigenous communities constitute 'indigenous peoples' for the purposes of grounding any rights under international human rights law. Setting aside whether or not the Arbitral Tribunals are the appropriate arbiters of this decision, the decision itself is clearly outside of the scope of the dispute before the Tribunals." [479]

2.4.2 Consistency: A Treaty May be Considered a Vehicle for the Application of Customary International Law

Treaties are sometimes conceived to be a supplementary/complementary instrument for applying customary international law. They may serve as mechanisms to apply and operationalize general international law in specific sub-fields or contexts, providing greater specificity and clarity to obligations that might otherwise be broad or general. Where a treaty is deemed to be a reflection, declaration, or codification (all these terms meaning effectively the same thing) of existing custom, the motivation for having a treaty may vary. Such rationales include providing stability through the general accessibility of legal texts (versus lack of clarity of uncodified custom), enhancing ideas of legality through the notice of the state of the law that comes with such accessibility, and providing institutional mechanisms for implementation or enforcement or interpretive norm development which mechanisms are generally absent for custom on its own.[480]

[478] *Ibid* para 59.
[479] *Ibid* para 60.
[480] On the final point regarding providing institutional mechanisms that custom is lacking, see the commentary on this treaty function in the ICJ's judgment in *Military and Paramilitary Activities in and against Nicaragua (Nicaragua v United States of America)*, International Court of Justice (ICJ), Judgment 26 November 1984.

In other instances, general customary international law may evolve overtime to become not only clearer but also more precise than the general expression of a treaty rule that originally reflected it at the time of the treaty's adoption.

Flowing from these conceptions and functions, there arises a general presumption that a treaty seeks in some way to either reflect, build on, or breed customary international law without conflicting with it. This consistent nexus suggests that treaties and customary international law often operate as complementary components of a unified legal framework, aligned toward common objectives and devoid of actual inconsistency. Consistency here refers to a legal idea that there is no actual conflict (an actor can comply with both sets of obligations). Here, treaty law is seen as reinforcing or codifying existing customary rules rather than contradicting them.

This consistency nexus suggests that treaties and customary international law often operate as complementary components that are needed to be harmonized through systemic interpretation where customary international law—notably, as it evolves—is used in the interpretation of treaty provisions ensuring coherence within the broader legal order. Consequently, this relationship necessitates a process of harmonization through systemic interpretation where customary international law—notably, as it evolves—informs the interpretation of treaty provisions ensuring coherence within the broader legal order.

In the adjudicative process, where the specific treaty norm and customary international law point in the same direction, "the specific rule should be read and understood within the confines or against the background of the general standard, typically as an elaboration, updating or technical specification thereof."[481] This is also true if we believe that the customary international law that existed at the time of the treaty's adoption is evolving and allowing later evolution of custom to influence the treaty's meaning. Unless the treaty explicitly states that the parties intended to "freeze" customary law at the time of adoption, the general presumption is that evolving customary international law can play a role in treaty interpretation even many years later. [482]

[481] Koskenniemi, *supra* note 406 at 19.
[482] Customary international law (CIL) is a living and adaptable source of international law, continuously shaped by state practice and *opinio juris*. While some argue that custom should remain fixed at the time of a treaty's adoption, the prevailing view among scholars and international courts is that CIL continues to evolve and can influence treaty

Courts would then use systemic interpretation to involve both bodies of law and interpret treaty provisions in harmony with general international law. This results in applying treaty law as a foundational legal framework for dispute resolution. And, as necessities arise, judicial authorities construe treaty law in juxtaposition with the broader spectrum of general law, of which treaties function as supplementary instruments.[483] However, it only works if the treaty is sufficiently ambiguous, general, or unclear to allow for multiple (at least two) reasonable interpretations. Otherwise, systemic interpretation cannot be used to rewrite a treaty when the meaning is already clear and directly contradicts a general international law rule. Customary law, in certain conditions, will be applied as an auxiliary legal framework to provide contextual background for treaty interpretation by furnishing the backdrop against which the treaty's provisions come to life:

> (a) The treaty rule is unclear and the ambiguity is resolved by reference to a developed body of general international law,
> (b) The terms used in the treaty have a well-recognized meaning in general international law, to which the parties can therefore be taken to have intended to refer, and
> (c) The terms of the treaty are by their nature open-textured and reference to general international law will assist in giving content to the rule.[484]

2.4.2.1 Case Law

Amoco International Finance Corporation v. Iran (1987) case law is an example whereby the tribunal interpreted the applicable treaty by referring to customary international law to decide on the lawfulness or unlawfulness of the exportation measures taken by Iran against the Amoco International Finance Corporation and interpret the treaty's provisions on compensation.[485] In this case, the tribunal effectively integrated customary international law. By doing so, it ensured that

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interpretation in its evolved content. See R Jennings & A Watts, eds, *Oppenheim's International Law* (Longman, Harlow, 1992); Higgins, *supra* note 413; Koskenniemi, *supra* note 406; Jean D'Aspremont, *Formalism and the Sources of International Law: A Theory of the Ascertainment of Legal Rules* (Oxford: Oxford Monographs in International Law, 2012). Such authors explain that customary law is a continuous process of legal formation and should not be artificially frozen at the time of a treaty's adoption.

[483] Koskenniemi, *supra* note 406 at 35.

[484] *Ibid* at 54.

[485] *Amoco International Finance Corporation v The Government of the Islamic Republic of Iran, National Iranian Oil Company, National Petrochemical Company and Kharg Chemical Company Limited,* Iran–United States Claims Tribunal Case No 56, Partial Award (Award No 310-56-3) 14 July 1987.

the treaty's application remained consistent with established international legal standards, particularly in defining expropriation and determining appropriate compensation for nationalized assets.

Amoco International Finance Corporation v. Iran

Before the Iranian Revolution, Amoco International Finance Corporation had entered into a contractual agreement with the National Iranian Oil Company (NIOC) for the exploration, development, and exploitation of petroleum resources in Iran. The agreement granted Amoco a concession to operate oil fields in exchange for sharing profits with Iran. In 1979, following the Iranian Revolution, the government of Iran implemented a policy of nationalizing foreign assets in the petroleum sector. This included Amoco's operations in Iran. The nationalization measures effectively terminated Amoco's contractual rights and interests in the oil fields. Amoco filed a claim before the Iran-United States Claims Tribunal, seeking compensation for the expropriation of its rights and interests in the Iranian oil fields. The company argued that the nationalization constituted an expropriation under international law, for which it was entitled to "prompt, adequate, and effective compensation." Iran defended the nationalization as a legitimate exercise of its sovereign right to control natural resources.

To decide on the lawfulness or unlawfulness of the exportation measures taken by Iran against the Amoco International Finance Corporation, both parties contended, and the tribunal agreed, that the lawfulness of the expropriation must be decided by reference to Article IV, paragraph 2 of the Treaty of Amity, Economic Relations, and Consular Rights between the United States and Iran that says:

> Property of nationals and companies of either High Contracting Party, including interests in property, shall receive the most constant protection and security within the territories of the other High Contracting Party, in no case less than that required by international law. Such property shall not be taken except for a public purpose, nor shall it be taken without the prompt payment of just compensation. Such compensation shall be in an effectively realizable form and shall represent the full equivalent of the

property taken; and adequate provision shall have been made at or prior to the time of taking for the determination and payment thereof.[486]

The claimant maintained that the expropriation was unlawful because it was contrary to the treaty, which in any case incorporated the rules of customary international law as a minimum standard. For their part, the respondent contended that any expropriation was made in conformity with international law, since it was the legitimate exercise of Iran's right to nationalize, such right being recognized by customary international law. Given the parties' contentions, the main issue to be discussed by the tribunal in this context related to the nature of the rules of customary international law to be applied in the interpretation of the treaty law.

The tribunal noted that, "the rules of customary law may be useful in order to fill in possible lacunae of the Treaty to ascertain the meaning of undefined terms in its text or, more generally, to aid interpretation and implementation of its provisions."[487] This approach allowed the tribunal to utilize customary international law to elucidate the treaty's provisions on expropriation and compensation. The tribunal then interpreted the term of "expropriation" included in the treaty of Amity, Economic Relations, and Consular Rights between the United States and Iran in light of the relevant customary international law As reflected in the Case Concerning Certain German Interests in Polish Upper Silesia (*Germany v. Poland*), 1926 P.C.I.J., Ser. A, No. 7, (Judgment of 25 May 1926) case law, the principles of international law generally accepted some sixty years ago in regard to the treatment of foreigners recognized very few exceptions to the principle of respect for vested rights. This case highlighted the necessity of distinguishing between lawful and unlawful expropriations, emphasizing that lawful expropriations must serve a public purpose and be accompanied by appropriate compensation: "expropriation for reasons of public utility, judicial liquidation and similar measures."[488] The tribunal observed that, over time, international law has evolved to universally recognize States' right to nationalize foreign property for a public purpose. This evolution reflects a shift from earlier, more restrictive interpretations to a broader acceptance

[486] *Treaty of Amity Economic Relations and Consular Rights between the United States and Iran*, 15 August 1955, 284 U.N.T.S. 93 (entered into force 16 June 1957), Article IV.
[487] *Amoco International Finance Corporation v. The Government of the Islamic Republic of Iran, National Iranian Oil Company, National Petrochemical Company and Kharg Chemical Company Limited,* Iran–United States Claims Tribunal Case No. 56, Partial Award (Award No. 310-56-3) 14 July 1987, *supra* note 485 para 112.
[488] *Ibid* para 113.

of nationalization, provided it aligns with public interest objectives and includes just compensation. The tribunal considered that this right was today unanimously accepted by the time of this dispute, even by States which reject the principle of permanent sovereignty over natural resources as the legal foundation of such a right to expropriate for a public purpose not limited to the reasons set out in *Germany v. Poland*. While the treaty outlines conditions for lawful expropriation, including the requirement for "just compensation," it does not specify the exact method for calculating such compensation. To address this, the tribunal turned to customary international law to define the standard and extent of compensation. The tribunal noted that terms like "prompt, adequate, and effective" or "full" are often used in international law to describe compensation, but interpretations vary widely. By referencing customary international law, the tribunal aimed to establish a fair and equitable compensation standard that reflects the treaty's intent and international legal principles.

Against this background, the tribunal asserted that the provisions of Article IV, paragraph 2 of the treaty must be read in accordance with customary law. Although the provisions are phrased in a negative form and emphasize the principle of the respect due to foreign property, they nevertheless amounted to a clear recognition of the right to nationalize. The tribunal then noted "in stating that '[s]uch a property shall not be taken except for a public purpose,' the Treaty implies that an expropriation which is justified by a public purpose may be lawful, which is precisely the rule of customary international law."[489]

Nasser Esphahanian v. Bank Tejarat (1983) case is another case brought before the Iran United States Claims Tribunal dealing with whether a claimant with dual Iran/United States nationality could bring a claim before the tribunal. In this case, the tribunal noted that the applicable treaty is silent about the definition of "nationality" and thus it determined the meaning of the text (nationality) by turning to general international law for interpretative guidance. This case underscores the critical role of customary international law as a gap-filling mechanism in treaty interpretation. Here, I am using gap-filling to refer to the reading of broadly worded provisions and not the other possible meaning—the more aggressive gap-filling of reading a customary norm into a treaty where a matter simply is not addressed (i.e. when there is a lacuna. It also

[489] *Ibid* para 115.

highlights the tribunal's commitment to upholding established international legal principles when treaties are silent, ensuring decisions are rooted in widely accepted norms. By invoking the principle of dominant and effective nationality from customary international law, the tribunal provided clarity on the interpretation of "national." This approach allowed the tribunal to assert jurisdiction over claims involving dual nationals, ensuring that individuals with a genuine and substantial connection to a state could seek legal remedies under the treaty.[490]

Nasser Esphahanian v. Bank Tejarat

In *Nasser Esphahanian v. Bank Tejarat* case, the claimant, Nasser Esphahanian, an individual with dual Iran-United States nationality, stated that he had been a U.S. national and was entitled to file a claim in the Iran-United States Claims Tribunal against Iranians the Bank, Bank Tejarat, seeking the payment of U.S. $ 704,691.85. The respondent, Bank Tejarat, contended that the tribunal has no jurisdiction over this claim, owing to the Iranian nationality of the claimant. Both parties agree that the tribunal's task was to determine whether Esphahanian's claim is within its jurisdiction as a claim of a national of the United States within the meaning of Article II(1) and Article VII (1) of the Claims Settlement Declaration. Article II(1) reads, in part, as follows:

> An international arbitral tribunal (the Iran-United States Claims Tribunal) is hereby established for the purpose of deciding claims of nationals of the United States against Iran and claims of nationals of Iran against the United States, and any counterclaim which arises out of the same contract, transaction or occurrence that constitutes the subject matter of that national's claim.[491]

Article VII (1) of the Declaration provides, in pertinent part, that:

> A "national" of Iran or of the United States, as the case may be, means (a) a natural person who is a citizen of Iran or the United States; and (b) a corporation or other legal entity which is organized under the laws of Iran or the United States or any of its states or territories, the District of Columbia or the Commonwealth of Puerto Rico, if, collectively, natural persons who are citizens of such country hold, directly or

[490] *Nasser Esphahanian v. Bank Tejarat,* Iran–United States Claims Tribunal, Case No 157, Award 29 March 1983, para 161.

[491] *Declaration of the Government of the Democratic and Popular Republic of Algeria Concerning the Settlement of Claims by the Government of the United States of America and the Government of the Islamic Republic of Iran (Claims Settlement Deceleration),* 19 January 1981, 75 A.J.I.L. 418 (1981), Article II (1).

indirectly, an interest in such corporation or entity equivalent to fifty per cent or more of its capital stock.[492]

In accordance with these articles, Esphahanian argued that the text is clear and unambiguous and that it applies to all nationals of the United States and of Iran, including dual nationals, without restriction. The Bank, in response, argued that Iran does not recognize dual nationality and could not be presumed to have accepted it when the Declaration was signed. However, the tribunal dismissed both arguments by nothing that "in the absence of any specific provision in the Claims Settlement on this point, the tribunal must determine the meaning of the text through use of the rules of the Vienna Convention. Paragraph 3(c) of Article 31 directed the tribunal us to take into account "any relevant rules of international law applicable in the relations between the parties."[493] In this context, the tribunal referred to Article 1 of the Hague Convention on Certain Questions Relating to the Conflict of Laws to underscore the principle that each state has the sovereign authority to determine its own nationals. Article 1 states: "It is for each State to determine under its own law who are its nationals."[494] It means essentially, each country decides who is considered a national under its own laws, but other countries must respect those decisions within the bounds of international law. This law shall be recognised by other States in so far as it is consistent with international conventions, international custom, and the principles of law generally recognized with regard to nationality.

This reference was pertinent in assessing the dominant and effective nationality of Mr. Esphahanian, to establish jurisdiction. By citing Article 1, the tribunal emphasized the importance of genuine connections in nationality claims, ensuring that state determinations of nationality are consistent with international legal standards. In applying international law, the tribunal found itself "in a position similar to that of a court of a third State faced with the claim of a dual national against one of the States of his nationality."[495] Therefore, it engaged Article 5 of the Hague Convention that explains "within a third State, a person having more than one

[492] *Ibid* Article VII (1).
[493] *Supra* note 490 para 23.
[494] *The Hugue Convention on Certain Questions relating to the Conflict of Nationality Laws,* 12 April 1930, Article 1.
[495] *Supra* note 490 para 28.

nationality shall be treated as if he had only one" and third States "may, in [their] territory, recognize exclusively amongst the nationalities possessed by such individual, either the nationality of the country in which he mainly and principally resides, or the nationality of the State to which, according to the circumstances, he appears to be more attached in fact."[496] This led the tribunal to adopt the notion of effective or dominant nationality. It "conclude[d] that this Tribunal has jurisdiction (a) over claims against Iran by dual Iran-United States nationals when the dominant and effective nationality of the Claimant is that of the United States and (b) over claims against the United States by dual Iran-United States nationals when the dominant and effective nationality of the Claimant is that of Iran."[497]

The European Court of Human Rights (ECtHR), in *McElhinney v. Ireland (2001)* case, also had recourse to customary international law, particularly in relation to the doctrine of state immunity that protects States from being sued in the courts of another State without their consent, in interpreting the European Convention on Human Rights (ECHR).[498] The *McElhinney* case illustrates how the ECtHR integrated customary international law into its interpretation of treaty provisions. By referencing customary international law, the ECtHR concluded that granting state immunity to the UK in this case did not violate Article 6(1) of the Convention.

McElhinney v. Ireland

Mr. McElhinney, an Irish national, was involved in an incident at the border between Ireland and Northern Ireland in March 1991. During this event, a British soldier, while inspecting McElhinney's vehicle, forcibly pushed Mr. McElhinney to the ground and allegedly assaulted him within the territory of the Republic of Ireland. In June 1993, McElhinney initiated legal proceedings in Ireland against the British soldier and the UK government, seeking damages for the alleged assault. In its defence, the United Kingdom argued that it could not be sued in Irish courts due to the principle of state immunity, which protects States from being subject to the

[496] *Supra* note 494 Article 5.
[497] *Supra* note 490 para 46.
[498] *McElhinney v Ireland,* European Court of Human Rights, Application No 31253/96, Judgment 21 November 2001.

jurisdiction of foreign courts in certain circumstances. The court ruled that under customary international law, States are generally immune from being sued in another State's domestic courts for actions performed in the exercise of sovereign authority even within the territory of the foreign State. The Irish court dismissed his claim, upholding the UK's assertion of sovereign immunity. This decision was later affirmed by the Irish Supreme Court.

Mr. McElhinney then appealed to the ECtHR, contending that the Irish courts' recognition of the UK's sovereign immunity violated his right to a fair trial as guaranteed the ECHR. The applicant argued that denying him the ability to pursue legal action in Ireland due to state immunity unjustly restricted his access to justice. He invoked, in particular, Article 6 of the ECHR, which provides:

> In the determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law. Judgment shall be pronounced publicly but the press and public may be excluded from all or part of the trial in the interests of morals, public order or national security in a democratic society, where the interests of juveniles or the protection of the private life of the parties so require, or to the extent strictly necessary in the opinion of the court in special circumstances where publicity would prejudice the interests of justice.[499]

Against this background, the ECtHR had to decide whether the application of state immunity violated Mr. McElhinney's right to access a court under Article 6(1) of the ECHR and whether the application of state immunity, as a rule of customary international law, in this context aligned with Article 6 of the ECHR in order to serve as a legitimate limitation on the right to access justice. In its assessment, the court observed that the right of access to court is not absolute but may be subject to limitations. Such limitations must, however, pursue a legitimate aim and be proportionate. These limitations should not restrict or reduce the access left to the individual in such a way or to such an extent that the very essence of the right is impaired. In addition, while limitations generally acknowledged by the community of nations as part of the doctrine of state immunity are legally acceptable, they will not be compatible with Article 6 if they do not pursue a legitimate aim and if there is no reasonable relationship of proportionality

[499] *Protocol to the Convention for the Protection of Human Rights and Fundamental Freedoms (European Convention on Human Rights) as Amended by Protocol No. 11, Council of Europe Treaty Series 155, Council of Europe, 1988*.

between the means employed and the aim sought to be achieved. To assess whether the limitation was proportionate to the aim pursued, the court recalled the Convention, including Article 6, cannot be interpreted in a vacuum. Indeed, "the Convention has to be interpreted in the light of the rules set out in the Vienna Convention of 23 May 1969 on the Law of Treaties, and that Article 31(3)(c) of that treaty indicates that account is to be taken of 'any relevant rules of international law applicable in the relations between the parties'."[500]

The tribunal then observed that there appears to be a trend in customary international towards limiting state immunity in respect of "insurable" personal injury caused by an act or omission within the forum State. Insurable personal injury includes incidents such as those arising out of ordinary road traffic accidents, rather than matters relating to the core area of State sovereignty such as the acts of a soldier on foreign territory, in this case foreign in the sense that the UK solder engaged in their conduct on Ireland's territory, which, of their very nature, may involve sensitive issues affecting diplomatic relations between States and national security. It followed that measures taken by a High Contracting Party that conform to generally recognised rules of public international law on state immunity cannot in principle be regarded as imposing a disproportionate restriction on the right of access to court as embodied in Article 6. The court clarified that "it cannot be said that Ireland is alone in holding that immunity attaches to suits in respect of such torts committed by *acta jure imperii* or that, in affording this immunity, Ireland falls outside any currently accepted international standards."[501] The ECtHR agreed with the Irish courts upholding the United Kingdom's claim to immunity cannot be said to have exceeded the margin of appreciation allowed to States in limiting an individual's right to access to court. It held that granting state immunity in the specific context of the case did not violate Article 6 because such immunity is a legitimate limitation on the right of access to a court. Thus, the ECtHR followed that there has been no violation of Article 6 in this case and the application of state immunity in this case was proportionate and pursued a legitimate aim, namely, to uphold principles of international law and state sovereignty.[502]

[500] *McElhinney v Ireland,* European Court of Human Rights, Application No 31253/96, Judgment 21 November 2001, para 36.
[501] *Ibid* para 38.
[502] *Ibid* para 40.

Cross-referencing customary international law, particularly in light of Article 31(3)(c) of the VCLT, also serves as an essential tool for treaty interpretation in investment law. Although investment law is considered a self-contained regime—an intricate web of more than 3,000 investment treaties with a distinct dispute settlement mechanism under the multilateral ICSID Convention—systemic interpretation keeps this regime interconnected and consistent with the broader framework of international law. *Sempra Energy International v. Argentina (2007)* is an illustrative example that shows how the investment tribunal involved customary international law in the treaty interpretation process. In this case, the tribunal explained that, since the applicable treaty "did not deal with the legal elements necessary for the legitimate invocation of a state of necessity," "rules governing such questions will thus be found under customary law."[503] The tribunal noted, because the applicable investment treaty lacked detailed provisions for addressing complex issues like state of necessity, it would rely on customary international law (as codified in the International Law Commission's Articles on Responsibility of States for Internationally Wrongful Acts) to assess the host State's plea of necessity. That is to say, there was a gap in the treaty on a general legal issue within the law of state responsibility and thus it fell to custom to fill that gap; as a corollary of this, silence in a treaty on an element of state responsibility law does not set aside that law but provides the basis for applying the custom to harmonize treaty and general international law.

Sempra Energy International v. Argentina

Sempra is a US investor that held an equity interest in Argentinean gas distribution companies in early 1990s. At that time, in order to attract foreign investors, Argentina enacted legislation to provide Sempra with incentives, among which it was guaranteed that tariffs for gas distribution would be calculated in US dollars until 2027. However, in the circumstances of the economic crisis, on 2 January 2002, Argentina enacted the "Emergency Law," which abrogated the right to calculate tariffs in US dollars ("pesification of tariffs"). It led to a very

[503] *Sempra Energy International v. Argentina,* ICSID Case No ARB/02/16, Award 28 September 2007, para 387.

substantial reduction in the profitability of the gas distribution business and, accordingly, returns on Sempra's investment.

In 2002, Sempra initiated ICSID arbitral proceedings claiming multiple violations of the 1991 Argentina-US BIT and requesting damages. Sempra argued that Argentina breached the standard of fair and equitable treatment established under Article II(2)(a) of the treaty.[504] Sempra also brought a claim about an alleged breach of the observance of the obligations into which Argentina entered with regard to the investment in the light of the umbrella clause of Article II(2)(c) of the treaty.[505] The tribunal found that the "measures in question in this case have beyond any doubt substantially changed the legal and business framework under which the investment was decided and implemented" and that, therefore, Argentina committed "an objective breach of the fair and equitable treatment due under the Treaty ... to the detriment of the Claimant's rights."[506] The tribunal also found that the measures taken by Argentina were far from "ordinary" contractual breaches; instead they were "the outcome of major legal and regulatory changes introduced by the State" and thus were in breach of the umbrella clause.[507]

In the event the tribunal found Argentina liable for breaching its obligations under the treaty, Argentina alternatively invoked an exemption from liability, arguing that the national emergency or state of necessity justified its actions. In particular, to justify Argentina's regulatory measures that would otherwise constitute breaches of its investment protection commitments under the treaty, Argentina put forth its plea of necessity based on Article XI:

> This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.[508]

[504] *Ibid* para 290.
[505] *Ibid* para 306.
[506] *Ibid* para 303.
[507] *Ibid* para 311.
[508] *Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment, signed November 14, 1991 (entered into force October 20, 1994)*, online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/127/download>.

To justify its regulatory measures under this Article, Argentina asserted that the significant decreases in the Argentine Gross Domestic Product, consumption and investment during the crisis period, together with deflation and the reduction in value of Argentine corporations, resulted in widespread unemployment and poverty, with dramatic consequences for health, nutrition and social policy. To overcome such difficulties, Argentina urgently resorted to a 2002 Emergency Law, which is legitimate under Article XI, to protect economic security and political stability, as well as classical military security.[509] In this context, although 2002 Emergency Law adversely affected Sempra, it was adopted by Argentinian government to protect the essential security interests of its country and maintain public order. Thus, Argentina cannot be liable to compensate Sempra.

The tribunal acknowledged the application of Article XI. However, it added that the Article did not deal with the legal elements necessary for the legitimate invocation of a state of necessity. Thus, in order to assess the state of necessity for removing Argentina's liability, the tribunal must resort to the requirements laid down in customary international law. The tribunal explained that "the treaty provision is inseparable from the customary law standard insofar as the definition of necessity and the conditions for its operation are concerned, given that it is under customary law that such elements have been defined."[510] The tribunal argued that since the treaty does not define what is to be understood by an "essential security interest," "the requirements for a state of necessity under customary international law … become relevant to the matter of establishing whether the necessary conditions have been met for its invocation under the Treaty. Different might have been the case if the Treaty had defined this concept and the conditions for its exercise, but this was not the case."[511]

The tribunal then relied on Article 25 of the ILC on Responsibility of States for Internationally Wrongful Acts (ARSIWA) "as reflecting the state of customary international law on the matter."[512] Article 25 states:

[509] *Sempra Energy International v. Argentina,* ICSID Case No. ARB/02/16, Award 28 September 2007, *supra* note 503 para 367.
[510] *Ibid* para 376.
[511] *Ibid* para 375.
[512] *Ibid* para 344.

1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:
(a) is the only way for the State to safeguard an essential interest against a grave and imminent peril; and
(b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.
2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:
(a) the international obligation in question excludes the possibility of invoking necessity; or
(b) the State has contributed to the situation of necessity.[513]

The tribunal made clear that it viewed a state of necessity as a most exceptional defence that is subject to very strict conditions, thus the state of necessity "may not be invoked" unless these conditions are met.[514] The tribunal initiated its assessment by examining whether the Argentine crisis qualified as one affecting an essential interest of the State. On this issue the tribunal noted that "the argument that such a situation [a severe financial crisis compromised the very existence of the State and its independence, and thereby qualified as one involving an essential State interest, is not convincing."[515] The tribunal then must decide about the alleged existence of a grave and imminent peril that could threaten the essential interest. On this matter, it argued that "while the Government had a duty to prevent a worsening of the situation, and could not simply leave events to follow their own course, there is no convincing evidence that events were actually out of control or had become unmanageable."[516] To decide whether the measures taken under the Emergency Law were the "only way" for Argentina to handle the economic crisis, the tribunal found that "there are always many approaches to addressing and resolving such critical events. It is therefore difficult to justify the position that only one of them was available in the Argentine case."[517] For determining whether the measures in question seriously impair the interests of a State or States toward which the obligations exist, or of the international community as a whole, the tribunal held that "[t]he interest of the international community does not appear to be in any way impaired in this

[513] International Law Commission (ILC), *supra* note 214 Article 25.
[514] *Sempra Energy International v. Argentina,* ICSID Case No. ARB/02/16, Award 28 September 2007, *supra* note 503 para 354.
[515] *Ibid* para 348.
[516] *Ibid* para 349.
[517] *Ibid* para 350.

context, as it is an interest of a general kind."[518] For the condition on whether Argentina had contributed to the situation giving rise to a state of necessity, the tribunal said "there has to some extent been a substantial contribution of the State to the situation giving rise to the state of necessity, and that it therefore cannot be claimed that the burden falls entirely on exogenous factors."[519] The tribunal then concluded "[i]n the light of the various elements examined above, the Tribunal concludes that the requirements for a state of necessity under customary international law have not been fully met in this case."[520]

2.4.3 Inconsistency: A Treaty May be Considered an Exception to Customary International Law

In the second scenario, treaty law and customary law point in inconsistent directions/obligations for dealing with the same set of facts. Inconsistency happens when "it is possible for a party to two treaties to comply with one rule only by thereby failing to comply with another rule."[521] This is the basic situation of inconsistency that needs a test of norm-by-norm actual conflict of obligations. Treaties can create *inter se* exceptions for or modifications to the existing rules of customary international law by deviating from certain requirements established by the customary international law. For most kinds of treaty, state parties to a treaty are permitted under the general international law on sources of law to decide to deviate from a rule of customary international law as amongst themselves even as they must continue to abide by the customary rule in their relations with third-party States that are not part of the specific treaty.[522]

Reasoning about the extent of permissibility of such deviation or exceptions depends on how the "genuine shared expectations of the parties, within the limits established by overriding community objectives" are defined with larger views about the purposes of the international legal system.[523] For instance, deviation is not permissible where the customary rule is a *jus cogens*

[518] *Ibid* para 352.
[519] *Ibid* para 354.
[520] *Ibid* para 355.
[521] Koskenniemi, *supra* note 406 at 13.
[522] See WTO Appellate Body report, *EC measures concerning meat and meat products (hormones)* (1998) para 120.
[523] Harold D Lasswell, James C Miller & Myres S McDougal, *The Interpretation of International Agreements and World Public Order: Principles of Content and Procedure* (New Haven and Martinus Nijhoff Publishers Dordrecht: New Haven Press, 1994) at 82.

one.[524] It is also not generally thought to be possible with respect to treaties that are humanitarian in nature—where interstate agreement creates the obligations but where the beneficiaries are not the States but persons protected by the treaties. For example, two States cannot by bilateral agreement relieve themselves of obligations under a human rights treaty to each other's nationals.

Here, treaty law is *lex specialis*, the idea that a special/smaller group of actors, based on the consent theory, carve out from generally applicable norms of custom. It means, although both treaty law and customary law have same subject matter, treaty law has more precise/specific norms that should be applied to the exclusion of customary international law on the specific norms, preventing states parties to that treaty from invoking that rule of customary international law. This point is clearly articulated by Thirlway who says, "[i]t is universally accepted that—consideration of *jus cogens* apart—a treaty as *lex specialis* is law between the parties to it in derogation of the general customary law which would otherwise have governed their relations."[525] Thus, the principle of consent-based exception requires that the reciprocal interests of the parties must be achieved by replacing customary norms and rendering them irrelevant for the treaty interpretation process.[526]

However, such replacement is partial and the general rule "remains in the background providing interpretative direction to the special one."[527] To further explore the relationship between *lex specialis* and general principles of international law, Koskenniemi argues that "most of general international law is dispositive and can be derogated from by way of exception. But an 'exception', too, works only in a relative sense so that whatever is being 'set aside' will continue to have an effect on the interpretation and application of the exception."[528] Accordingly, it should be noted that in confrontation with the idea of exception (set aside, carve out), there is a difference between one body of norms derogating from another body of norms and one individual obligation excepting from another individual obligation (one each from a body of norms). So, at

[524] Mahmoud, "International Crimes: Jus Cogens and Obligation Erga Omnes" (1996) 59 Law and Contemporary Problems 63–74.
[525] Hugh Thirlway, "The Law and Procedure of the International Court of Justice 1960–1989 (Part One)" (1989) 60 British Yearbook of International Law at 174.
[526] International Law Commission (ILC), *supra* note 214.
[527] Koskenniemi, *supra* note 406 at 56.
[528] *Ibid*.

minimum, the way to make sense of the notion of a set aside even as the set aside does not vanish altogether is to be clear that one obligation setting aside another obligation does not oust the ongoing interpretive relevance of the body of law to which the set-aside norm belongs as it would still inform interpretation of other non-conflicting treaty provisions.

2.4.3.1 Case Law

In the *EC Measures Concerning Meat and Meat Products (Hormones) (1998)* case within the World Trade Organization (WTO), the European Community argued that the precautionary principle, which it considered to have the status of customary international law, should be used to interpret Article 5.1 and Article 5.2 of the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (SPS Agreement).[529] The European Community argued that this interpretive approach provided a legitimate basis for its prohibition on the importation of certain meat and meat products treated with specific growth hormones. However, the WTO Appellate Body rejected the use of the precautionary principle for interpreting the SPS Agreement, notwithstanding acknowledging that the principle may have evolved into customary international law. The Appellate Body concluded that: "we consider that this principle [precautionary principle] would not override the explicit wording of Articles 5.1 and 5.2 outlined above, in particular since the precautionary principle has been incorporated and given a specific meaning in Article 5.7 of the SPS Agreement."[530] This case thus represents two examples of custom's relationship to a treaty. One relationship is the treaty as incorporating some elements custom (art. 5.7) and the other relationship is the treaty departing from other elements of the custom (Article 5.1 and 5.2, and the specific meaning in Article. 5.7).

[529] United Nations Conference on Environment and Development (UNCED), *Rio Declaration on Environment and Development* (1992), online: <https://www.un.org/en/development/desa/population/migration/generalassembly/docs/globalcompact/A_CONF.151_26_Vol.I_Declaration.pdf> Resolution 1, Annex I; *Agreement on the Application of Sanitary and Phytosanitary Measures, The World Trade Organization, 15 April 1994,* online: < https://www.wto.org/english/docs_e/legal_e/15-sps.pdf>.

[530] *European Communities – Measures Concerning Meat and Meat Products (Hormones) (EC — Hormones),* WT/DS26/AB/R and WT/DS48/AB/R, Appellate Body Report 13 February 1998, para 120.

European Communities – Measures Concerning Meat and Meat Products (Hormones)

In 1996, the United States and the Canada brough a panel before the Dispute Settlement Body (DSB) of the World Trade Organization (WTO) complaining that the European Communities' prohibition of imports of meat and meat products derived from cattle violated the Agreement on the Application of Sanitary and Phytosanitary Measures (SPS Agreement). In particular, they argued that such measures were in breach of Article 5 of the SPS Agreement on Assessment of Risk and Determination of the Appropriate Level of Sanitary or Phytosanitary Protection:

> 1. Members shall ensure that their sanitary or phytosanitary measures are based on an assessment, as appropriate to the circumstances, of the risks to human, animal or plant life or health, taking into account risk assessment techniques developed by the relevant international organizations.
>
> 2. In the assessment of risks, Members shall take into account available scientific evidence; relevant processes and production methods; relevant inspection, sampling and testing methods; prevalence of specific diseases or pests; existence of pest- or disease-free areas; relevant ecological and environmental conditions; and quarantine or other treatment.[531]

On 18 August 1997, the US Panel Report and the Canada Panel Report reached the same conclusions and stated that "The European Communities, by maintaining sanitary measures which are not based on a risk assessment, has acted *inconsistently* with the requirements contained in Article 5.1 of the Agreement on the Application of Sanitary and Phytosanitary Measures [SPS Agreement]."

On 24 September 1997, the European Communities notified the DSB of its decision to appeal certain issues of law covered in the Panel Reports and certain legal interpretations used by the Panels. The European Communities submitted that the precautionary principle is already, in the view of the European Communities, a rule of customary international law, and the essence of which applies in the assessment of risk under Articles 5.1 and 5.2 of the SPS Agreement. The European Communities asserted that Articles 5.1 and 5.2 of the SPS Agreement do not prescribe a particular type of risk assessment, but rather simply identify factors that need to be

[531] note 529 Article 5.

taken into account. Thus, the European Communities argued that the precautionary principle, which permits States to adopt protective measures even in the absence of full scientific certainty about the potential risks to human health or the environment, should be used in interpreting the SPS Agreement. The European Communities invoked "the precautionary principle in support of its claim that its measures in dispute are based on a risk assessment. To the extent that this principle could be considered as part of customary international law and be used to interpret Articles 5.1 and 5.2 on the assessment of risks as a customary rule of interpretation of public international law."[532] By invoking this principle, the European Communities sought to align its regulatory measures with both Articles 5.1 and 5.2 and rules of customary international law dealing with the subject matter of risk prevention and the protection of public health, such that Articles 5.1 and 5.2 needed to be read to harmonize with the customary international law rules.

The Appellate Body noted that although the European Communities argued that the precautionary principle is part of customary international law and should be used to interpret Articles 5.1 and 5.2, this principle would not override the explicit wording of the SPS Agreement. The Appellate Body acknowledged that the precautionary principle might have become part of customary international law. However, the Appellate Body pointed out the inconsistency of the precautionary principle with the SPS Agreement. It emphasized that, "the [precautionary] principle has not been written into the SPS Agreement as a ground for justifying SPS measures that are otherwise inconsistent with the obligations of Members set out in particular provisions of that Agreement."[533] The Appellate Body further explained that Article 5.2 of the SPS Agreement demands SPS measures "take into account available scientific evidence" while the European Communities' ban was found to lack a proper scientific risk assessment to substantiate the claimed health risks from hormone-treated meat.

The Appellate Body then affirmed "the ultimate conclusion of the Panel that the EC import prohibition is not based on a risk assessment within the meaning of Articles 5.1 and 5.2 of

[532] *European Communities – Measures Concerning Meat and Meat Products (Hormones) (EC — Hormones),* WT/DS26/AB/R and WT/DS48/AB/R, Appellate Body Report 13 February 1998, *supra* note 530 para 120.
[533] *Ibid* para 124.

the *SPS Agreement* and is, therefore, inconsistent with the requirements of Article 5.1."[534] It agreed with the finding of the Panel Reports that the precautionary principle does not override the provisions of Articles 5.1 and 5.2 of the SPS Agreement:

> We thus find that the precautionary principle cannot override our findings made above, namely that the EC import ban of meat and meat products from animals treated with any of the five hormones at issue for growth promotion purposes, in so far as it also applies to meat and meat products from animals treated with any of these hormones in accordance with good practice, is, from a substantive point of view, not based on a risk assessment.[535]

The Appellate Body's decision reflected that the SPS Agreement has its own cautionary approach and State Members "establish their own appropriate level of sanitary protection" that needs "scientific evidence" and is more specific than the general precautionary principle under the customary international law.[536] In this respect, the Appellate Body found the customary norm irrelevant to be used for interpreting Article 5 of the SPS Agreement and thus the precautionary principle, could not displace the specific and binding commitments under WTO agreements. It then concluded that: "we consider that this principle [precautionary principle] would not override the explicit wording of Articles 5.1 and 5.2 outlined above, in particular since the precautionary principle has been incorporated and given a specific meaning in Article 5.7 of the SPS Agreement."[537] Accordingly, the Appellate Body found the customary international law irrelevant to be used for interpreting the SPS Agreement.

2.5 Take-Away on the Relevance of (Transnationalized) Customary International Law in ISDS Tribunals

This chapter develops a comprehensive framework for how ISDS tribunals are likely to determine substantive law in investment disputes. After elucidating the central role of IIAs and the limited role of domestic law, I primarily focus on the pivotal role of international law—particularly customary international law—in dispute resolution procedures. The focus then shifts to the critical function of customary international law, particularly in relation to how it interacts

[534] *Ibid* para 208.
[535] US Panel Report, paras. 8.157-8.158; Canada Panel Report, paras. 8.160-8.161.
[536] *European Communities – Measures Concerning Meat and Meat Products (Hormones) (EC — Hormones),* WT/DS26/AB/R and WT/DS48/AB/R, Appellate Body Report 13 February 1998, *supra* note 530 para 124.
[537] *Ibid* para 120.

with treaty law in the context of investment dispute settlement. This interaction lies at the heart of the chapter's inquiry—specifically, whether transnational self-regulated norms, if they were recognized as transnationalized customary international law, impose environmental obligations on investors can be invoked by ISDS tribunals as a relevant rule to resolve, or contribute to the resolution of, the substantive aspects of investment treaties.

Article 31(3)(c) of the VCLT obliges tribunals to take into account "relevant rules of international law applicable in the relations between the parties," which includes customary international law. To help legal practitioners and arbitrators assess whether transnational self-regulated norms qualify as "relevant," this chapter proposes a two-step analytical framework grounded in flexibility and practicality:

1. Transnational self-regulated norms must address the same subject matter as that of the investment treaty being interpreted.
2. Transnational self-regulated norms requirements must be consistent with the obligations set forth in the treaty.

The first step in incorporating customary international law through systemic interpretation is to determine whether both the treaty provision and the customary rule address the same legal issue or regulatory concern. Where such subject-matter overlap exists, systemic interpretation can be employed to ensure coherence between treaty obligations and the broader framework of international law. If, however, treaty and custom relate to distinct subject matters, systemic interpretation sounds futile; forcing such integration risks obscuring conceptual distinctions and undermining legal clarity.

The second step evaluates whether consistency exists between the treaty provision and the customary norm. If no actual conflict arises, systemic interpretation facilitates the harmonization of the treaty with customary international law. But in cases of conflict, a consent-based *lex specialis* approach is applied: the more specific treaty norm prevails over the general customary norm, reflecting the priority given to the consent of the treaty parties. Even so, the customary rule is not erased entirely—it remains interpretively relevant in shaping the meaning of non-conflicting provisions.

Ultimately, this framework seeks to promote clarity and stability in ISDS reasoning by offering a principled method to determine when and how transnational self-regulated norms—as expressions of transnationalized customary international norms—may be invoked in treaty interpretation. The next chapter builds on this analysis by examining whether transnational self-regulatory norms can be recognized as "applicable" transnationalized customary international law within the interpretative framework of investment treaties.

Chapter 3: Theoretical Framework for the Legal Status of Self-Regulated Norms as Transnationalized Customary International Law

3.1 Introduction

> "Although not all law is privately made, and most privately made law depends ultimately on the power of the state—power the state lends, dependably and in generous measure—enough law is privately made that we should care."[538]

International investment law is an ongoing struggle over creating viable and enforceable norms to foster sustainable development at the transnational level while protecting the interests of both States and foreign investors. In particular, the sustainable development/investment nexus became visible in the late 1990s when environment-related investment disputes began to be filed with investor-state dispute settlement (ISDS) tribunals that are assumed to be the primary international forum to strike a balance between investment protection and environmental considerations.[539] Think of the way in which the creation of these tribunals is intended to foster foreign investments: it is a reflection of the continuous effects that the Western domination of global history seems to have on both law creation and enforcement within the investment sector. Under this hegemony, ISDS tribunals, although superficially suggesting formal equality of States, continue to protect mostly foreign investors from developed countries with the project of resolving investment disputes based on international rules, in most cases international investment agreements (IIAs), that are created in a world historically divided by deep power differentials. In addition to the fact that IIAs do not impose environmental obligations on foreign investors but only safeguards their protective rights, host Sates are not permitted to take environmentally protective actions that violate investors' rights. That means if host States take actions, such as passing laws requiring that environmental impact assessments be conducted in connection with

[538] Nicole Roughan, "From authority to authorities: bridging the social/normative divide" in Roger Cotterrell & Maksymilian Del Mar, eds, *Authority in Transnational Legal Theory: Theorising Across Disciplines* (Northampton, MA: Edward Elgar Publication, 2016).
[539] Miles, *supra* note 108.

decisions about permitting particular foreign investments or that investment be allowed only if compatible with sustainable development principles, such actions "must be enacted and implemented in accordance with the investment treaty's obligations; because the treaty's obligations are thereby triggered, an investor can then challenge the manner in which a State implements environmental protections or other measures directed toward protecting human rights."[540] In most cases, as my case law analyses in Chapter 1 reveal, ISDS decisions ensuing from contests between investors' protective rights and environmental measures of host States are regarded as disfavoring goals of sustainable development. This discloses the failure of international investment law to take into consideration foreign investors' environmental responsibilities.

To address this gap and advance environmental accountability within ISDS tribunals—and building on the findings of Chapter 2, which demonstrate the important role that international legal norms do and can play in resolving the substantive dimensions of investment disputes—I take two key steps aimed at expanding the scope of substantive international law in ISDS proceedings. First, I go beyond the Western-domination, international-lawmaking approach whereby foreign investors are not only protected as the primary purpose of the international investment law regime but additionally exonerated from incurring international obligations. Second, I examine the legal status of transnational self-regulated norms that are created beyond the state-centric notion of law so as to be capable of imposing international environmental obligations on foreign investors to resolve substantive aspects of investment disputes.

Regarding the first concern, which was thoroughly discussed in Chapter 1, IIAs, as the central substantive international law in the dispute settlement process, do not strike a balance between the rights and obligations of disputing parties to the extent that host States are the primary entities responsible for safeguarding the economic rights of investors through ensuring a stable regulatory environment that promotes investment protection and economic growth. The flipside is that

[540] Andrea K Bjorklund, "Sustainable Development and International Investment Law" in Kate Miles, ed, *Research Handbook on Environment and Investment Law* (Edward Elgar Publishing, 2019) 38 at 39.

foreign investors are the entities that enjoy protective rights without being either nationally or internationally responsible to host States.[541]

To this end, I embrace a more expansive understanding of investors (notably, corporations) as actors both involved in lawmaking and subject to obligations (not only rights) attendant upon the kind of actor they are and the kind of activities that international law permits them to engage in. I then take the second step—more or less seamlessly with the first step as they are analytically intertwined—to recognize transnationalized customary international law norms capable of imposing direct international environmental obligations on foreign investors as applicable rules of international law. This requires examining whether these norms are opposable to those suffering harm (whether States or non-state)—thereby creating not only a defence for state measures but also causes of action to hold investors environmentally responsible at the transnational level. When I say at the transnational level, I am taking the form of law to remain international law but the substance to be transnationalized—a reworking of public international law from within itself to accommodate more lawmaking participants, as well as obligations running between those participants.

My entry point to this discussion, alongside the *Urbaser* case, is the *Nevsun Resources Ltd. v. Araya (2020)* case.[542] To briefly recall, the *Urbaser* case shows foreign investors could be targeted of transnational self-regulated norms in the context of the human rights protection and such norms can be recognized as substantive rules of international law applicable to investment disputes. The award in this case stands out for two reasons: 1) it provides the first attempt where the issue of foreign investors' human rights obligations in the operation of an economic activity was decided on the basis of international law; and 2) soft law instruments were extensively taken into consideration for the purposes of determining the international human rights obligations of

[541] In Chapter 2, it is discussed that foreign investors are required to comply with national law only at the establishment stage of investment activities—in order to thereby be considered as legally protected activity in ISDS tribunals. And since investors are not recognized as traditional subjects of international law, they are not traditionally assumed to be directly obliged by rules of international law.
[542] *Nevsun Resources Ltd v Araya,* Supreme Court of Canada, Case No 37919, Judgment 28 February 2020.

foreign investors.[543] Likewise, in *Nevsun Resources Ltd. v. Araya*, the Supreme Court of Canada, for the first time, held that customary international law arguably binds companies and permits judicially determined civil remedies—including through domestic courts—for victims of a corporation's customary international law violations.[544]

The plaintiffs, Eritrean workers, claimed that Nevsun, a Canadian mining company, breached customary international law in its use of forced labour, slavery, cruel, inhuman or degrading treatment, and crimes against humanity, where alleged use could extend to either direct involvement of the company or forms of complicity with the State of Eritrea. The plaintiffs sought damages from Nevsun under customary international law as incorporated into the law of Canada. Nevsun argued, however, that even if customary international law norms such as those relied on by the Eritrean workers form part of the common law through the doctrine of adoption, those norms create obligations for States and not a corporation and, additionally any obligation that might exist for a given norm would not be opposable to the corporation by other private actors as a private-law cause of action without a specific customary international rule providing as such. Nevsun explained that States are the primary subjects of international law and thus international law (including customary international law) only binds state conduct. Accordingly, Nevsun sought to have the case dismissed in part through a motion of no reasonable cause of action—with respect to the customary international law claims.[545] However, the Supreme Court of Canada quoted the motions judge saying that "[t]he proceeding raises issues of transnational law," which challenged the court to decide about the potential corporate liability for alleged breaches of customary international law.[546] Despite the four full or partial dissents in the case that corporations cannot be held liable for alleged breaches of international legal norms, according to the majority in a 5-4 decision, the

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[543] *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, *supra* note 3; Giovanna Adinolfi, "Soft Law in International Investment Law and Arbitration" (2021) 1:1 The Italian Review of International Law and Comparative Law 86–112.
[544] Russell Hopkins, "Introductory Note to Nevsun Resources LTD. V. Araya et al. (S.C.C.)" (2020) 59 The American Society of International Law.
[545] They did not challenge the causes of action framed in traditional domestic-law categories on the basis of no reasonable cause of action. They did try the act of state doctrine, which was rejected at all levels.
[546] *Nevsun Resources Ltd. v. Araya,* Supreme Court of Canada, Case No. 37919, Judgment 28 February 2020, *supra* note 542 para 67.

Supreme Court of Canada held that a non-state actor can be held liable for its breaches of customary international legal norms.[547]

In this context, I intend to examine whether transnational self-regulated norms—which are developed within the investment sector and through constant interactions between States and non-state actors—could be treated as "rules of international law *applicable* in the relations between the parties," under Article 31(3)(c) of the Vienna Convention on the Law of Treaties (VCLT), and then be involved in resolving substantive issues arising before ISDS tribunals.[548] By means of this analysis, I will propose that transnational self-regulated norms imposing environmental obligations on foreign investors not only cannot be ignored but must be treated as applicable transnationalized customary international law that ISDS tribunals may apply to hold foreign investors environmentally responsible at the transnational level. Applicability, which is the critical word in this analysis, would at the least require tribunals to assess whether an investor has abided by those obligations. It is used here in the sense of transnational self-regulated norms that are both *opposable* as between and legally *binding* on the disputing parties in order to be involved in the treaty interpretation process.[549] As Prezas defines, "opposability simply means that a legal subject is bound by a rule or act of international law. For instance … a rule of customary international law is opposable *erga omnes*, i.e., it is binding all States."[550] This definition explains why the terms *opposable* and *binding* are used interchangeably and as synonyms most of the time, while *applicability* captures the two together.

Therefore, in this chapter, instead of favoring "the comfort of conviction over the discomfort of doubt," I challenge the traditional/state-centric notion of international law to examine the process through which transnational self-regulated norms can become rules of transnationalized

[547] See Section 3 for the comprehensive discussion on the direct liability of the foreign investors under international law.
[548] note 4.
[549] The basis for opposability is that international legal obligations are not merely aspirational or voluntary; they have legal force and can be invoked by other States or international entities to ensure compliance and seek remedies when violations occur. This concept is essential for maintaining order and accountability in the realm of international relations and ensuring that States adhere to their commitments under international law, Eirik Bjorge, "Opposability and Non-Opposability in International Law" (2021) British Yearbook of International Law 1–38.
[550] Ioannis Prezas, "A Bilateral Treaty Developing Legal Effects Erga Omnes? Reflections on the Prespa Agreement Between Greece and North Macedonia Settling the Name Dispute" (2020) 65 Questions of International Law 21–61 at 48.

customary international law opposable to and legally binding on foreign investors.[551] To investigate whether transnational self-regulated norms can become invokable as transnationalized customary international law that the mainstream investment and arbitral law community would feel justified, or even obliged, to fold into their interpretation of existing IIAs, I will study the most complex and essential questions about the legal status of transnational self-regulated norms:[552]

- Which actors have relevant lawmaking powers in transnational self-regulated norms (institutional structure)?
- How do transnational self-regulated norms become legitimate law (normative structure)?

These questions direct me to articulate this chapter through a four-pronged analysis that suggests a necessary rethinking of the sources and subjects of international law. The need to rethink the foundational structures of international law emanates from recognizing the shortcomings of the traditional international lawmaking process in resolving the substantive aspect of investment disputes to protect both the foreign investors' interests and host States' environmental values. Such recognition leads to strong doubt about the capacity of States to regulate the globalized world on their own (i.e., through traditionally-conceived, purely interstate lawmaking processes) and thus to an inquiry into the importance of self-regulated norms in governing transnational interactions. Admittedly, my approach requires having sufficient faith in the capacity of ISDS tribunals to strike a balance between investors' protective rights and their environmental responsibilities. This requires ISDS to recognize that traditionally conceived forms of applicable law may be insufficient to address issues that transcend national boundaries. I acknowledge that some may view this confidence as a leap of faith. However, I maintain a broader conviction that reasoned and well-supported argumentation has the potential to shift perspectives—even among traditionally resistant actors. It is from this position of critical doubt that I reexamine the established knowledge surrounding international lawmaking, while proceeding with a measure of confidence in the pursuit of new insights.

[551] Adam Grant, *Think Again: The Power of Knowing What You Don't Know* (New York: Viking, 2021) at 4.
[552] See the comprehensive discussion on "applicable law" in ISDS tribunals in Chapter 2.

In the face of these accumulating doubts, for the first prong, I set a background to discuss how *self-regulated norms* called soft law, originating neither in the nation-state nor exclusively from within non-state organizations, are surfaced in the globalized economy to manage transnational interactions among States and non-state actors. To better understand the definition of soft law, I use the concept of transnational law to fundamentally challenge traditional (state-centered) approaches to lawmaking for governance of the globalized economy. However, soft law understood in this sense still faces challenges both to be considered as rules of international law and then to be applied in ISDS tribunals. In a nutshell, this directs my study towards recognizing soft law as *transnationalized customary international law* capable of being treated as applicable law to substantive issues in ISDS tribunals.

With a shift in the terrain of sociolegal research, transnational law remains such an imprecise notion that its characteristics are debated in many fundamental respects. In the second prong of analysis, I use *legal pluralism* to explain that non-state actors could become involved in the transnational lawmaking process and discuss the possible creation of law that are in some measure from below, born out of social interactions among States and non-state actors. By putting it this way, legal pluralism studies transnational legal governance in a globalized context whereby multiple lawmaking powers pursue their interests through communal interactions that develop transnational self-regulated norms. Alongside reviewing key scholarly contributions on legal pluralism, I also discuss the legal reasonings of the *Urbaser* and *Nevsun* cases to discuss how non-state actors could be internationally obliged by rules of international law.

A clarifying comment is important here: "self-regulated" is used in full realization that the involvement of States (albeit to different extents in different contexts) and the fact of sectoral interactions amongst many individual corporate actors mean these norms are not fully "self"-regulatory either in the sense of not being imposed by States or in the sense of arising solely from the volition of individual corporate actors. As such, "partially self-regulated" might be the more accurate term, even as I will stick to "self-regulated" for ease of expression.[553] This leads to my next point in hybridity.

[553] Additionally, I will use "self-regulated" and "self-regulatory" interchangeably.

The emergence of transnational self-regulated norms as central to a transformative regulatory framework becomes attractive to study theoretically in terms of their legal status as transnationalized customary international law. The third prong of analysis is an exploration of the question of "who are relevant lawmaking powers in transnational self-regulated norms?," I use the *hybrid theory* developed by Calliess and Zumbansen as a promising new approach to describe and assess the institutional aspect of the transnational lawmaking regime.[554] Neither explicitly public nor private and originating neither solely in the nation-state nor exclusively from within international organizations, the hybrid theory sheds light on how the transnational lawmaking process is a dynamic regulatory framework for the engagement of non-state actors with States.

To deepen my theoretical analysis, the fourth prong studies the question, "How do transnational self-regulated norms become legitimate?" I turn to the *interactional theory* as articulated mostly by Brunnée and Toope as a process-oriented approach for examining the normative aspect of transnational self-regulated norms.[555] By means of this theory, legitimacy of transnationalized customary international law is not simply generated via interstate consent (nor, for that matter, by inter-corporate consent). Instead, these norms should attain legitimacy through a complex process of appraisal—one that involves both those who have participated in their creation and those who are affected by their application (either as direct addressees of obligations or as third-party sufferers of harms).

This four-pronged analysis is a fruitful approach for understanding and contributing, in a reflective way, to the legal discourse evolving around the lawmaking role of transnational actors and the legal status of transnational self-regulated norms—a discourse that occurs in both the scholarly realm and in the world of professional practice. It guides me to explore obstacles to effective transnational norm creation, where public and private actors mostly compete but sometimes cooperate in authoritative governance. My analysis also reveals avenues through which critical actors and especially authoritative decision-makers could recognize a given self-

[554] Gralf-Peter Calliess & Peer Zumbansen, *Rough Consensus and Running Code: A Theory of Transnational Private Law* (London: Hart Publishing, 2010).
[555] Jutta Brunnée & Stephen J Toope, *Legitimacy and Legality in International Law: An Interactional Account* (Cambridge, UK; New York: Cambridge University Press, 2010).

regulated norm or set of norms as legitimate to the point of the norm/s crystallizing as applicable law. This analysis has practical significance for demonstrating whether and how transnational environmental initiatives, such as the United Nations Global Compact, can become invokable as *applicable* transnationalized customary international law—that is, be opposable to and binding for foreign investors—that ISDS tribunals either must or may apply to resolve substantive aspects of investment disputes.

3.2 Globalization

In the 1970s, with the emergence of anti-colonial movements and the rise of developing States, mainly in Asia and Africa but also in industrial societies, skepticism was cast over the portrayal of States as the sole lawmaking power.[556] Later, in the 1980s, Walker refers to globalization as an extension of economic activities beyond national borders and advances in international transactions to such an extent that the state-centric foundations of legal orders is challenged.[557] Clapham explains that the globalization of the world economy has highlighted the power of large corporations in a sense that "decision-making is conducted away from national parliaments and under the influence of powerful states ... [and that] the realization that large multinationals may not only control more resources than the smallest states, but that corporate global influence can overwhelm local cultures and initiatives."[558] Berman similarly affirms that in the globalized economy, States are no longer the ultimate law-making power; instead, "nation-states must work within a framework of multiple, overlapping jurisdictional assertions by state, international, and even nonstate communities."[559] It thus becomes clear that a single-minded focus on state-to-state relations was inadequate to describe the reality of the globalized market economy. In its place, as Santos explains, States and non-state actors interact in complex social fields:

> The nation-state and the interstate system are the central political forms of the capitalist world system, and they will probably remain so for the foreseeable future. What has happened, however, is that they have become an inherently contested terrain, and this is

[556] Michael Barry Hooker, *Legal Pluralism: An Introduction to Colonial and Neo-Colonial Laws* (Oxford: Clarendon Press, 1975) at 52; Franz von Benda-Beckmann & Keebet von Benda-Beckmann, "Legal Pluralism and Legal Anthropology: Experiences from Indonesia" in *Pluralism, Transnationalism and Culture in Asian Law* (Singapore: ISEAS Publishing, 2017) 70 at 71.
[557] Neil Walker, *Intimations of Global Law* (United Kingdom: Cambridge University Press, 2014) Global Law Series.
[558] Andrew Clapham, *Human Rights Obligations of Non-State Actors* (Oxford University Press, 2006) at 4.
[559] Paul Schiff Berman, *Global Legal Pluralism: A Jurisprudence of Law Beyond Borders* (Cambridge: Cambridge University Press, 2012) at 7.

> the central new fact on which the analysis must focus: the state and the interstate system as complex social fields in which state and non-state, local and global social relation interact, merge and conflict in dynamic and even volatile combinations.[560]

These dynamic and volatile combinations are surfaced when state sovereignty has declined in importance, and as a result of which myriad transnational non-state actors—intergovernmental organizations, nongovernmental organizations, and corporations—are serving as transnational decision makers who interact with nation-state governance to regulate transnational activities through transnational self-regulated norms.[561] Transnational self-regulated norms emerge from networked structures of international organizations, civil society actors, and private corporations to regulate the globalized economy and compensate for market failure to protect socio-environmental values. These norms, which depart from a lawmaking process that strictly relies on traditional diplomatic actors and are developed mostly through interaction between States and non-state powers to provide standards of conduct for business enterprises, are considered as "soft law" or "informal" law under traditional international law accounts.[562]

3.2.1 Transnational Self-Regulated Norms (Soft Law)

Globalization complexifies international law to the extent that the traditional international hard law would not be enough to accommodate the growing complications of international relations. Soft law then comes into the scene to play an important part in international regimes: "formal

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[560] B de S Santos, *Toward a New Legal Common Sense: Law, Globalization, and Emancipation* (London: Butterworths LexisNexis, 2002).

[561] Harold Hongju Koh, "Transnational Legal Process and the 'New' New Haven School of International Law" in Jeffrey L Dunoff & Mark A Pollack, eds, *International Legal Theory Foundations and Frontiers* (Cambridge University Press, 2022) 101.

[562] Pauwelyn and his collaborators, in *Informal International Lawmaking*, at 2, name self-regulated norms as informal rules of international law: "Firstly, in terms of output, international cooperation may be 'informal' in the sense that it does not lead to a formal treaty or any other traditional source of international law, but rather to a normative output that is not part of the traditional sources of either domestic or international law. Secondly, in terms of process, international cooperation may be 'informal' in the sense that it occurs in a loosely organized network or forum rather than a traditional treaty-based [intergovernmental organization]. Thirdly, in terms of actors involved, international cooperation may be informal in the sense that it does not engage traditional diplomatic actors." Although defining self-regulated norms as informal rules is correct, in this study, I call them "soft law" as it is extensively addressed in the literature. Soft law norms are not included as a traditional source of international law under Article 38(1) of the Statute of the International Court of Justice; non-state actors have been particularly active in their development, thus skewing from the traditional lawmaking process that strictly relies on state power; and their adoption process has also differed from other rules that are either developed by States or attained by States' consent. These characteristics bear important implications regarding the potential use of self-regulated norms to address environmental concerns in ISDS tribunals through the principle of systemic integration, as provided in Article 31of VCLT.

decision-making and binding rules stand alongside a panoply of … soft law" to govern transnational economic activities among States and non-state actors.[563] In this picture, "formal international law is often sidelined or replaced by 'informal law-making' through soft law, standards, guidelines, best practices, or recommendations which, though nonbinding in form, often elicit high compliance among their addressees."[564]

Across legal fields, the turn to soft law is ubiquitous, and unsurprisingly, definitions for this development abound to the point that "soft law means different things to different people."[565] Most importantly, in 2000, Chinkin[566] summarized six definitions of soft law norms that all focus on explaining what soft law is in terms of contrasts to traditionally conceived law. Soft law norms (1) are articulated in non-binding form (e.g., in an instrument that is itself considered non-binding)—such as General Assembly resolutions that are characterized by the UN Charter as "recommendations"—or in an instrument that is formally binding as a whole but where a specific treaty provision softens the obligation to the point of expressing it as desirable versus required as when a treaty states that parties "should," not "must," do X);[567] (2) contain only vague or imprecise obligations;[568] (3) emanate from institutions or entities that lack formal law-making

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[563] United Nations Human Rights Council, *Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy" Framework* (2011), online: <https://www.ohchr.org/sites/default/files/documents/publications/guidingprinciplesbusinesshr_en.pdf>.

[564] Nico Krisch, "Global Legal Pluralism" in Jeffrey L Dunoff & Mark A Pollack, eds, *International Legal Theory: Foundations and Frontiers* (Cambridge University Press, 2022) 240 at 257.

[565] Gunther F Handl, "A Hard Look at Soft Law: Remark" (1988) 82 Proceedings of the Annual Meeting (American Society of International Law) 371–395 at 371. For a comprehensive discussion on different approaches towards soft law, see Felix Dasser, "'Soft Law' in International Commercial Arbitration" (2019) 402 Collected Courses of the Hague Academy of International Law and Jacob E Gersen & Eric A Posner, "Soft Law" (2008) *University of Chicago Public Law and Legal Theory Working Paper* No 213.

[566] Christine Chinkin, "Normative Development in the International Legal System" in Shelton Dinah L, ed, *Commitment and Compliance: The Role of Non-Binding Norms in the International Legal System* (Oxford; New York: Oxford University Press, 2000).

[567] In my supervisor's view, Professor Craig Scott, "such softness can extend to the binding force of decisions of institutions that are created by treaties and empowered by the treaty to direct a decision towards States. A leading example would be the 'views' the Human Rights Committee can issue in response to individual communications under the Optional Protocol to the International Covenant on Civil and Political Rights (ICCPR). At the start of this protocol almost 50 years ago, it was non-controversial that these 'views' did not create a duty to obey on the part of a given State found by the Committee to have breached an ICCPR provision but rather were in the nature of a non-binding finding. Over time, ideas of good faith compliance with treaty obligations and acquiescence in the interpretive authority of the Committee have led the Committee, some States and many academic commentators to say that the dichotomy of binding/non-binding is not a suitable frame and that there is some 'hardness' to the duties to respond in good faith to Committee views—although there is no consensus that evolution has proceeded to the point of those 'views' being understood now as binding *per se.*"

[568] This version of soft law can be formally legally binding by virtue of their source—notably, treaties—but it is the generality of their content that makes them "soft." It is thus also common for such soft law to be left for future law-

authority; (4) originate from or are directed at non-state actors; (5) whose violation does not trigger the legal responsibility of States under the rules of state responsibility (that is, they lack any corresponding theory of responsibility; whose breach does not constitute an "internationally wrongful act"); or (6) elicit only voluntary adherence and rely upon non-judicial means of enforcement.

Ten years later, Guzman and Meyer[569] along with Jacob and Schill[570] define what soft law has rather than what it lacks as compared to hard law. Instead of characterizing soft law as merely the absence of binding force or enforceability, they emphasize its positive attributes—namely, its capacity to influence behavior, shape expectations, and impact legal or policy decision-making. They suggest soft law is comprised of a delimited set of techniques, rules, or instruments that have some kind of legal impact on decision-makers. For example, instruments such as the Carbon Disclosure Project (CDP) and the Equator Principles (EPs) offer several techniques for climate change management within the private investment sector that demonstrate how soft law can have a profound legal and practical impact. These instruments may not come with formal enforcement mechanisms let alone mechanisms the participants treat as legal enforcement, but they influence environmental decision-making through mechanisms like reputational incentives, normative alignment, peer pressure, and anticipatory compliance with emerging hard law.[571] Guzman and Meyer further explain the role of soft law in international law as "[n]onbinding rules or instruments that interpret or inform our understanding of binding legal rules or represent promises that in turn create expectations about future conduct."[572] Jacob and Schill then add that soft law as "[n]on-mandatory or discretionary legal techniques …can nevertheless impact decision-makers."[573]

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clarifying processes, such as through new protocols to a treaty that "harden" the norms over time—and such empowering certain institutions clarify content through interpretation. That said, soft law can be simultaneously "soft" in both the substantive sense of (2) and one or more of the other formal senses of (1), and (3)-(6).

[569] "Nonbinding rules or instruments that interpret or inform our understanding of binding legal rules or represent promises that in turn create expectations about future conduct," Andrew T Guzman & Timothy L Meyer, "International Soft Law" (2010) 2 Journal of Legal Analysis 171 at 174.

[570] Marc Jacob & Stephan W Schill, "Going Soft: Towards a New Age of Soft Law in International Law?" (2014) 8:1 World Arbitration and Mediation Review at 3.

[571] See Haniehalsadat Aboutorabifard, *Equator Principles and Climate Change Issues: Examining the EPs' Climate Change Policies and Analyzing the Likely Effectiveness of these Policies* (Masters Thesis, University of Waterloo, 2016).

[572] Guzman & Meyer, *supra* note 569 at 174.

[573] Jacob & Schill, *supra* note 570 at 3.

As can be inferred from the foregoing definitions, soft law is a multi-faceted concept that is applied to a variety of instruments and about which there is no clear consensus as to its definition. Indeed, it appears to be polyvocal in the sense of having the potential to mean different things in different contexts and usages. Therefore, some commentators consider soft law dangerous and a fundamental threat to the rule of law.[574] In their opinion, law is by definition binding and thus soft *law* is non-existent *as law* due to its non-binding status.[575] In contrast, others would accept that soft law is a relevant category in international law[576] and advances the rule of law by recognizing the complexity of its modern-day sources.[577]

For the purpose of this study, I aim at defining transnational self-regulated soft law as rules of international law that 1) fall outside the traditional formal sources of international law recalled in Article 38 of the international court of justice (ICJ)'s Statute, 2) are created out of interactions between States and non-state actors, and 3) shape international actors' behaviour as much as binding rules established under international agreements or customary international law. Against this framework, in the next section, I use the transnational law perspective to understand global lawmaking regime that regulate actions transcending national frontiers.

3.2.2 Transnational Law

To understand the evolving regulatory framework of transnational self-regulated soft law, the idea of transnational law was initially put forth by Jessup, in 1956, to introduce lawmaking on a global level as a branch of jurisprudence not only distinct from but also more comprehensive than state-centered (including interstate) law. At its most general, Jessup defines transnational law as "law which regulates actions or events that transcend national frontiers."[578] This definition is followed by an expansion of the traditional lawmaking framework based entirely on domestic

[574] Jan Klabbers, "The Redundancy of Soft Law" (1996) 65 Nordic Journal of International Law 167.
[575] Prosper Weil, "Towards Relative Normativity in International Law?" (1983) 77 American Journal of International Law 413.
[576] Adelle Blackett, "Global Governance, Legal Pluralism and the Decentered State: A Labor Law Critique of Codes of Corporate Conduct" (2001) 8:2 Indiana Journal of Global Legal Studies 401–447; Melvin Aron Eisenberg, "The Divergence of Standards of Conduct and Standards of Review in Corporate Law" (1993) 62:3 Fordham Law Review 437–463.
[577] Chris Brummer, *Soft Law and the Global Financial System: Rule Making in the 21st Century* (Cambridge: Cambridge University Press, 2015).
[578] Philip Caryl Jessup, *Transnational Law* (New Haven CT: Yale University Press, 1956) at 2.

(State) and international (interstate) constructs of law to include "other rules which do not wholly fit into such standard categories."[579] Ultimately, Jessup introduces the notion of "transnational law," "instead of 'international law'," as an inclusive category for all law involved in the regulation/governance of the issues that transcend national frontiers, whether involving States or non-state actors.

Jessup offers international lawyers a compelling proposal that is both theoretical as well as practical to find a way of expanding traditional legal understanding in order to address effectively and coherently the growing variety of border-crossing relations around the world. On the one hand, he encourages international lawyers to adopt a pragmatic view of the nature of transnational problems and the evolving landscape of relevant norms that are drawn upon, invoked, or created in response to these problems. On the other hand, the increasing complexity of border-crossing problems arising among States and non-state actors provided a good enough reason for Jessup to develop a theoretical view thereby "the traditional divisions between public international law and private international law and even some national law might be submerged in an ocean of 'transnational law'."[580] Therefore, by directing lawyers towards a recognition of a wider variety of relevant norms in border-crossing institutional interaction and, at the same time, an engagement with tension among competing normative orders, transnational law needs to be approached so as to "deal out jurisdiction in the manner most conducive to the needs and convenience of all members of the international community."[581]

This understanding of transnational law that breaks the mirror of a legal conception associating law too easily with States and scrutinizing the norm-creation process under the traditional lawmaking framework is further emphasized by Scott in "'Transnational Law' as Proto-Concept: Three Conceptions."[582] He notes that "transnational law" is an idea that pushes the boundaries of the traditional legal theory based entirely on domestic law and international law to go beyond current conceptual comfort zones about what counts as law as a matter of theory and how law-

[579] *Ibid* at 2.
[580] *Ibid* at 63.
[581] *Ibid* at 71.
[582] Craig M Scott, ""Transnational Law" as Proto-Concept: Three Conceptions" (2009) 10:7 German Law Journal 859.

invoking actors approach norms in practice. Scott elaborates that what is transcended in "transnational law" is "State" and, more importantly, its legal systems.[583] Therefore, "transnational law can variously connote law across states, law beyond states, or law through states (i.e. states' legal systems)"[584] and "'transnational law' in the sense of not being statist [would] involve multiple actors (who admittedly may owe their legal existence to state and interstate legal orders but who are nonetheless neither states nor interstate entities)."[585] Cotterrell also embraces these points that the concept of transnational law considers non-state-based norms as a potential source of law and also includes both States and non-state actors in the lawmaking process:

> [B]ecause all of these types and sources of law (as well as debates and disagreements about the specifically 'legal' quality of some of them) are involved, the best term to apply provisionally to the whole unwieldy mass seems to be transnational law, insofar as this regulation addresses, with some kind of claim of legal authority, individual persons (including corporations) across the boundaries of state jurisdiction. Some writers prefer to speak of postnational law but it must be stressed that, in the transnational picture, state and nation have in no way disappeared from view, nor is it foreseeable that they will. They are merely supplemented as sources and sites of law, but the transnational is not a world 'after' or 'outside' the state or the nation.[586]

Likewise, Koh weaves some New Haven School perspectives[587] into his Transnational Legal Process School to further explain what distinguishes transnational law from international law is its process and its substance.[588] By focusing on law as a process of authoritative decision-making (the fundamental New Haven approach to law), transnational law is "nontraditional – cutting across historical private/public and domestic/international dichotomies – and non-statist, inasmuch as the actors studied were not just, or even primarily, nation-states."[589] Koh also notes that the substance of transnational law "transcends old dichotomies between international and domestic law and between public and private law… transnational public law concepts are

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[583] *Ibid*.
[584] *Ibid* at 866.
[585] *Ibid* at 875.
[586] Roger Cotterrell, "Transnational Legal Authority: A Socio-Legal Perspective" in Roger Cotterrell & Maksymilian Del Mar, eds, *Authority in Transnational Legal Theory: Theorising Across Disciplines* (Northampton, MA: Edward Elgar Publishing, 2016) at 261.
[587] In the following page, I discuss the New Haven School of international law to further explain the idea of *legal pluralism*, the notion that multiple communities for law's development, interpretation and enforcement can make transnational law matter.
[588] Harold Koh, "The 1994 Roscoe Pound Lecture: Transnational Legal Process" (1996) 75:1 Nebraska Law Review.
[589] Koh, *supra* note 561 at 112.

emerging, rooted in shared national norms and emerging international norms that have similar or identical meaning in every national system."[590] This transnational legal process is then constituted of self-regulated norms (soft law), which seek not simply to ratify existing law as state or interstate sources would have it but to elevate a wider variety of international norms to the status and function of law.[591]

To discuss transnational law in a more pragmatic context, *lex mercatoria* is considered by Berman as an illustrative example of transnational norms that provide a vital means to meet the challenges of globalization in the economic sector.[592] Increased economic interconnectedness of States across the globe, along with eroded boundaries between national and international law resulted in the inability of steady domestic legislatures to keep pace with the increasing speed and sophistication of the globalized market economy. The fact that international businesspeople perceive domestic laws and courts to be unable to meet their legitimate expectations of legal certainty and predictability of the normative orders governing their deals has resulted in the private "bottom-up" systems of self-regulation developed through communal interactions among merchants, ship owners, insurance underwriters, bankers and others—whether they act as individuals, corporate entities, or as state agencies.[593] The resulting *lex mercatoria* encompasses various principles and provide a framework for resolving disputes and conducting transactions across borders.

The emergence of *lex mercatoria*, a "different legal order than that of States, which are only one type of legal order, with the special feature that it is territorially confined,"[594] predominantly

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[590] *Ibid* at 114.
[591] Note how this formulation shares much conceptual space with the traditional source of public international law, that of "general principles of law." While this dissertation focuses on the emergence of transnationalized customary international law, and does not as such explore general principles of law as a stand-alone source or component of transnational legal normativity, the idea of a kind of juridical influence of "concepts...that have similar or identical meaning in every national system" is a fruitful ground for future work on how one looks for the legal or juridical quality of claimed transnational customary norm—whether one uses a traditional idea like *opinio juris* or the idea of legitimacy that is the focal point in this dissertation.
[592] I am limiting myself to *lex mercatoria* in the contemporary sense and not engaging in debates about what historic forms of *lex mercatoria* (or the law merchant) were or were not.
[593] Harold J Berman, "The Law of International Commercial Transactions (Lex Mercatoria)" (1987) 2 Emory Journal of International Dispute Resolution 235.
[594] Jan Hendrik Dalhuisen, "Globalization and the Transnationalization of Commercial and Financial Law" (2013) 67 Rutgers Law Journal 19 at 20.

depends on trade usages which are increasingly codified by private entrepreneurs such as the International Chamber of Commerce. But it is also affected by international law[595] and in beneficial relationship with national law, for example, through commercial actors' continuous use of standard forms and similar contract clauses, which are constantly adapted to the changing needs of international business.[596] While the *lex mercatoria*, similar to other private ordering mechanisms that "take place in the shadow of national law,"[597] has important public aspects, "often state law is not what shapes and guarantees these mechanisms in practice, nor does it necessarily produce or even recognize the regulatory forms seen as binding by those subject to them."[598] This means that, even if *lex mercatoria* developed essentially by "private" actors such as traders in transnational commercial networks or corporations and corporate groups, it has "public" governance aspects that go beyond a mere compromise of private interests in transnationally operating groups or networks. Indeed, the *lex mercatoria*—developed not only through business custom (and state acquiescence in and judicial embrace of such custom) but also through private arbitration practice that leads this constellation of norms to sometimes be described as an autonomous transnational commercial law—involves "a continuous competition and interplay between state and non-state institutions."[599] It then reveals a very complex regulatory method that leads to a need for legitimacy—of this method and analogous ones in other transnational contexts—to be examined.[600]

This governance structure of the global economy makes international lawyers concerned with the critical role of self-regulated norms in managing transnational economic activities. I join the conversation put forth by Alvarez according to which, "irrespective of their formally nonbinding status on non-parties, these manifestations of soft law cannot be ignored by international lawyers and, at the very least, form a subsidiary source of international obligation as much as any

[595] Lisa Bernstein, "Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms" (1996) 144 University of Pennsylvania Law Review 1765.
[596] Roger Cotterrell, "A Legal Concept of Community" (1997) 12:2 Canadian Journal of Law & Society 75.
[597] Calliess & Zumbansen, *supra* note 554 at 117.
[598] Roger Cotterrell, "What Is Transnational Law?" (2012) 37 Law and Social Inquiry 500 at 509.
[599] Ralf Micheals, "The True Lex Mercatoria: Law Beyond the State" (2007) 14:2 Indiana Journal of Global Legal Studies at 465.
[600] Cotterrell, *supra* note 598 at 511.

'judicial opinion' identified in Article 38 of the ICJ's Statute,"[601] to discuss the role of soft law in investment dispute procedures and whether soft norms could become *applicable* law in ISDS tribunals to resolve the substantive aspects of investment disputes. For this object, in the next section, I examine the challenges that international lawyers will face when it comes to the application of transnational self-regulated norms (soft law) in ISDS tribunals.

3.2.3 Challenges for the Application of Soft Law in ISDS Tribunals

Several legal scholars, such as Wälde, Alvarez, and Ali, have discussed the application of soft law with respect to substantive issues in ISDS tribunals. On this basis, non-binding instruments have been relied on "as a lever for a recalibration of investment law and its interaction with competing rights and interests, including the protection of human rights or of the environment."[602] Wälde contends that since IIAs are "inherently ambiguous, in need of interpretation and without settled interpretative jurisprudence … international tribunals will rarely if ever reject reference to international standards … A competent counsel can therefore no longer … neglect relevant instruments of soft-law, either those that advance one's party's position or those that are adduced by the opponent."[603] In "Reviewing the Use of 'Soft Law' in Investment Arbitration," Alvarez notes "there is considerable evidence that, like it or not, publicly available ISDS rulings refer to what most commentators would consider being soft law, and that in some cases, these references matter to the outcome."[604] He refers to a soft law norm as a non-legally binding norm that has some legal impact on interpreting or informing our understanding of otherwise binding legal rules. For example, soft law is applied in ISDS tribunals "when arbitrators cite non-binding principles issued by an international organization or professional associations (whether these are designated as 'declarations,' 'recommendations,' 'guidelines,' or 'codes of conduct'), and even if these norms are not backed by the consent of states and emerge from and address non-state actors (such as the non-state participants involved

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[601] Jose E Alvarez, "International Organizations: Then and Now" 100 American Journal of International Law 324, at 328.
[602] Adinolfi, *supra* note 543.
[603] Thomas W Wälde, "International Standards in Transnational Investment & Commercial Disputes: The Role of International standards, Soft Law, Guidelines, Voluntary and Self-regulation in International Adjudication, Negotiation and Other Forms of Dispute Management" (2004) 1:4 Transnational Dispute Management (TDM) at 5.
[604] Jose E Alvarez, "Reviewing the Use of "Soft Law" in Investment Arbitration" (2018) 7:2 The European International Arbitration Review at 2.

in ISDS)."[605] Likewise, Ali discusses in "The Application of Non-State-Based Standards in International Arbitration," that non-state standards increasingly influence the outcome of decisions in ISDS tribunals.[606] This means that although soft law is not expressly one of the sources of international law set out Article 38 of the ICJ's Statute, this does not mean that it is not an additional source of law. The Statute's wording goes back over a century to the ICJ's Statute, was directed at what a pinnacle world court issuing binding judgments can consider qua law, and never purported to be an exhaustive list of sources of law for all legal contexts (let alone for all time). Soft law can indeed be applied as substantive law in ISDS tribunals to provide guidance on issues such as sustainable development and, in particular, environmental protection.[607]

Against this background, the *Urbaser v. Argentina* case is an example where substantive soft law was used by the ISDS tribunal. Recall the earlier discussion in Chapter 1. In *Urbaser*, soft law instruments were referenced by the host State to assert the existence of international obligations upon foreign investors in the performance of their economic activities. During the proceedings, the respondent submitted a counterclaim alleging the breach by the investor of its obligations, in particular the failure to make an investment so as to make it possible to guarantee the enjoyment of the human right to water by the population of the area affected by the concession. The tribunal examined whether private corporations can be under human rights obligations as a matter of international law and, if so, whether a relevant obligation such as to the right to water and sanitation applied to the claimant as contended by Argentina.

In its decision, the ISDS tribunal relied heavily on soft law instruments. In the first place, the tribunal paid attention to the UN Guiding Principles on Business and Human Rights as the "basic

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[605] *Ibid* at 13.
[606] Shahla Ali, "The Application of Non-State-Based Standards in International Arbitration" in Paul Schiff Berman, ed, *The Oxford Handbook of Global Legal Pluralism* (Oxford University Press, 2020).
[607] Article 38 of the Statute of the International Court of Justice reads as follows:

> 1. The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply:
> a. international conventions, whether general or particular, establishing rules expressly recognized by the contesting states;
> b. international custom, as evidence of a general practice accepted as law;
> c. the general principles of law recognized by civilized nations;
> d. subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law.

document" for international law standards on corporate social responsibility, including human rights commitments to be complied with in businesses' operations.[608] It then referred to other instruments: the 1948 UN Universal Declaration of Human Rights (UDHR), whose Article 30 was interpreted as imposing also upon multinational corporations a duty not to act in disregard of human rights; the 2010 UN General Assembly Resolution on the Right to Water and Sanitation, where it is recognized that the right to clean and safe drinking water is essential for the full enjoyment of all human rights; a general comment by the UN Committee on Economic, Social and Cultural Rights acknowledging the importance of the right to water and sanitation for the effective enjoyment of the right to an adequate standard of living under the 1966 International Covenant on Economic, Social and Cultural Rights; the International Labour Organization (ILO) Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, according to which all parties concerned by the document should respect the 1948 Universal Declaration and the corresponding international covenants. It also raised the UN Global Compact that requires business to "support and respect the protection of internationally proclaimed human rights" as a document which is premised on not being binding in the formal sense and is characterized by the soft nature of the expectation to incorporate human rights into the investor's operations.[609] On this ground, the tribunal concluded that "the human right for everyone's dignity and its right for adequate housing and living conditions are complemented by an obligation on all parties, public and private parties, not to engage in activity aimed at destroying such rights."[610] Accordingly, the tribunal held that there are some international law obligations that apply to foreign investors and not only States.

Nonetheless, the *Urbaser* decision—along with the attempts by Wälde, Alvarez, and Ali to justify the invocation of soft law by ISDS tribunals—remains on tenuous ground, especially among legal scholars who are critical of the relevance and authority of soft law within the framework of international arbitration. Since soft law does not hold the stable anchor of monism whereby the State is the sole actor to create and legitimize law, Klabbers and his positivist

[608] *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic,* ICSID Case ARB/07/26, Award 8 December 2016, *supra* note 3 para 1195.
[609] Kevin Crow & Lina Lorenzoni Escobar, "International Corporate Obligations, Human Rights, and the Urbaser Standard: Breaking New Ground?" (2018) 35:87 Boston University International Law Journal.
[610] *Urbaser S.A. and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic,* ICSID Case ARB/07/26, Award 8 December 2016, *supra* note 3 para 1199.

fellows reject its application in international tribunals.[611] Klabbers argues that, since soft law emanates from sources outside of States and is not backed by formal state consent, it should not be applied by tribunals that are charged only with passing on state responsibility for acts in breach of binding law.[612] Thus, "the soft law argument is not a very good argument indeed, not before a court, and not elsewhere either ... [N]ot only do we not need soft law, we don't even want it either. Soft law ... serves no identifiable purpose ... is, actually, detrimental ... And it misleads in that it suggests that law can come in varying shades: harder and softer."[613] Klabbers also adds that "the decisions … demonstrate that, to the extent that soft law instruments are applied by international tribunals, they are somehow recast into the more accepted sources of international law: treaties and custom."[614] Therefore, soft law *per se*, is not, in his view, capable of being applied in tribunals unless it transforms into hard—as in, traditionally sourced—law.

Klabbers' arguments are based on a strong statist legal formalism. But even a leading proponent of the more fluid New Haven School of international law, Reisman, objects to soft law's usage – not on the basis of a formalistic understanding of all law as statist (like Klabbers) but on the basis of functional differentiation of contexts in which soft law is (and is not) useful or otherwise appropriate. Reisman argues that arbitrators should not use soft law because they must respect specific party consent, and only material that the litigants agree to can be considered by the adjudicator. He notes "'soft law instruments' are also useful to the law jobs of some government officials, as a phase in preparing internal constituencies, both governmental and non-governmental, for eventual adoption of the same instruments as law. But for those who perform the specialized jobs of international judge or arbitrator and for those who entrust their lives and treasure to them, soft law should be off-bounds."[615] Although Reisman believes international actors deliberately choose a softer form of legalization—as superior institutional arrangements—that "represents some reinforcement of the legal symbol and, at least, prevents or retards the use

[611] This is a more specialized or uncommon use of "monism" by Klabbers and his fellows. More commonly, "monism" refers to the unity of public international law and domestic state systems in one legal order (versus "dualism" that sees them as separate).
[612] Klabbers, *supra* note 574.
[613] *Ibid*.
[614] *Ibid* at 174.
[615] Gabrielle Kaufmann-Kohler, "Soft Law in International Arbitration: Codification and Normativity" (2010) 1 International Journal of Dispute Settlement 282 at 284.

of violence to achieve aims,"[616] he notes arbitrators should not use soft law, mainly because arbitration is a constrained process that needs to respect specific party consent and only traditional rules of international law *applicable* between parties can be considered by the adjudicator.[617]

Likewise, some legal scholars criticize the *Urbaser*'s award due its reference to soft law for resolving the substantive issues of the case. In contrast to Alvarez's observation that "*Urbaser* is a good example of … soft law used as a tool to 're-balance' the interests of investors and respondent states under IIAs,"[618] the *Urbaser* decision has been harshly challenged by other international law scholars for conferring such validity and importance to human rights arguments that, to them, constitute soft law. For example, given the voluntary nature of the United Nations Global Compact, Abel denounces that the tribunal's resorts to this non-binding source of human rights norms to prove a legally binding international human rights obligation of investors.[619] It was also mentioned that the tribunal did not explain how the UDHR—which is not a treaty—would create legally binding international rights and obligations. For Abel, given the lack of status as sources of international law as reflected in Article 38(1) of the ICJ's Statute, these non-binding norms establish by themselves an international obligation of investors. Furthermore, the tribunal is criticized for lacking any argument on how these non-binding norms could have acquired a binding status or could reflect binding international law.

Scholars like Klabbers, Reisman, and Paul have arguably criticized the application of soft law in the dispute settlement procedures not only due to the incompatibility of soft law with their theories of law but also because of the scarcity of scholarship on the role of non-state actors in the international law-making process and the lack of suggestive normative theoretical frameworks for analyzing self-regulated norms as a subfield of international law.[620] In response

[616] W. Michael Reisman, "A Hard Look at Soft Law" (1988) 82 American Society of International Law Proceedings 371 at 377.
[617] Reisman, *supra* note 616.
[618] Alvarez, *supra* note 604 at 50.
[619] Patrick Abel, "Counterclaims Based on International Human Rights Obligations of Investors in International Investment Arbitration: Fallacies and Potentials of the 2016 ICSID Urbaser v. Argentina Award" (2018) 1:1 Brill Open Law 61–90.
[620] Admittedly, this applies mostly to Klabbers and Paul. Reisman's centrality to the New Have School for half a century means he can hardly be said to be unaware of such scholarship as exists—indeed, he has contributed to it. It

to these critics and in support of awards applying soft law in ISDS tribunals, I direct the remaining sections of this chapter towards recognizing soft law as transnationalized customary international law capable of being applied to substantive issues in ISDS tribunals.

3.2.4 Self-Regulated Norms (Soft Law) as Transnationalized Customary International law

In my opinion, the criticism of the idea of applying soft law in ISDS tribunals arises in part from the way in which state-centrism dominates both in terms of understanding what actors can produce law and what kind of norms can count as law. First of all, soft law itself seems mostly to be understood in a state-centric understanding of law. What is non-binding or too imprecise to be a manageable standard focuses on the inadequacy of the claimed obligation to be law but it still tends to take for granted that their source—soft as it is—is one form or another of state-centered norm-making—the idea soft law norms also emanate in part from the involvement of civil or corporate actors in law-making tends to not even be considered. Second, international law is stuck in a highly positivistic (i.e. state-positivism not the more pluralistic social-fact-positivism) understanding of what law necessarily must be and this naturally shapes the reaction to efforts to apply soft law in interpreting IIAs in a non-positivistic account of where law can come from.[621] Confining international law to the sources included in Article 38 of the ICJ's Statute and defining soft law according to what it lacks as compared to hard law directs international adjudicators to apply only traditional rules of international law, including treaties, custom, or general principles, in the investment dispute tribunals.

To circumvent such criticisms and articulate my contribution towards proposing soft law norms as *applicable* law in ISDS tribunals, I seek to recognize these norms as transnationalized customary international law reflecting interactions among States and non-state actors in the globalized economy. This means that instead of sticking to the positivist assumptions of international law and identifying soft law in contradistinction to Article 38 of the ICJ's Statute as "*not* state-centric, *not* coercively enforced, *not* precise,"[622] I recognize soft law as

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may thus be most accurate to say that the lack of critical mass of scholarship on these topics as they apply to the investment realm is a contributing factor, not a general scarcity.

[621] Jean D'Aspremont, "International Legal Positivism" in Jeffrey L Dunoff & Mark A Pollack, eds, *International Legal Theory: Foundations and Frontiers* (Cambridge University Press, 2022) 63.

[622] Alvarez, *supra* note 604 at 5.

transnationalized customary international law that is developed by authorized lawmaking powers and legitimized by the subjects of the norms. Such recognition, as explained by Muniz-Fraticelli, introduces soft law as norms that "claim to possess—and attempt to exercise—a measure of legitimate authority over their members, and assert that this authority does not derive from the magnanimity of a liberal and tolerant state but is grounded, rather, on the common practices and aspirations of those individuals who choose to take part in a common endeavor."[623] In addition, aligned with Scott's third conception of transnational law, such norms "can be treated as other than national or international in the sense of a body of law that gradually takes on a certain internal coherence in the form of a hybrid synthesis appropriate to a given normative subject-matter and surrounding context."[624] Such norms would have a legal impact while operating on their own terms without the necessity of being fully incorporated within (or as) state-centric hard law.[625]

For the sake of this contribution, I have to go beyond the state-centric notion of law that fails to take account of transnational governance developments that emerged due to the rise of non-state actors and non-state-based norms. In this journey, I respect Wälde, Alvarez, and Ali and follow their perspective: "many ISDS rulings would simply not make sense without considering the contribution of soft law to their rationales and sometimes to the results reached… [and] an international investment lawyer who does not examine soft law would be doing a disservice to her client."[626] However, by arguing that soft law on its own can be transnationalized customary international law capable of being applied in ISDS tribunals, I will present substantial arguments for why investment arbitrators have to apply relevant transnational norms in their decision-

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[623] Victor M Muniz-Fraticelli, *The Structure of Pluralism: On the Authority of Associations* (Oxford: Oxford University Press, 2014) at 1. In my supervisor's view, this way of expressing things aligns closely with sociological or social-fact positivism, whereby the law can arise from a combination of felt need underpinning a collective or a common project for governance rules and of the involvement of different societal actors beyond States or interstate organizations. That is to say, one can be a positivist of a more inclusive and pragmatic sort than the state-centered variety—an orientation that will dovetail with this chapter's later discussion of pluralist approaches to law. See for discussion of social-fact positivism at the intersection of the pluralist socio-legal theory with respect to international/transnational legal personality Scott, *supra* note 472.

[624] Scott, ""Transnational Law" as Proto-Concept", *supra* note 582 at 874.

[625] Julia Black & David Rouch, "The Development of Global Markets as Rule- Makers: Engagement and Legitimacy" (2008) 2:3 Law and Financial Markets Review 218–233; Peer Zumbansen, "Where the Wild Things Are: Journeys to Transnational Legal Order, and Back" (2016) 1:1 University of California Irvine Journal of International, Transnational, and Comparative Law 161.

[626] Alvarez, *supra* note 604 at 18.

making—rather than only to issue "sensible decisions" or provide "service to clients." At the same time, there is also a threading-the-needle dimension to my effort as I also validate the criticisms that IIAs should be interpreted in light of rules of international law (Klabbers) and that investment arbitrators must meet parties' expectations in the dispute settlement process (Reisman). However, in contrast to Klabbers and Reisman, instead of rejecting the role of soft norms in ISDS tribunals, I introduce them via the notion of rules of transnationalized customary international law, which are created by States and non-state entities in response to the emerging expectations of the globalized world and thus can be legitimately treated as *applicable* law in resolving substantive issues of investment disputes.

It worth noting here that many legal scholars discuss various ways through which soft law could have practical implications and be respected in international law.[627] Concerning the state-centric notion of law, they explain how soft law could be transformed into hard law in the future and then attempt to persuade international arbitrators to apply them when there were hardened. However, this approach is different from that of mine explained above in that I do not seek to demonstrate that soft law has become interstate customary international law understood in the most traditional sense. Rather, in light of changes in the globalized world, I introduce soft law as *transnationalized customary international law* that, in its current arrangement, should be applied in ISDS tribunals. In the former instances, soft norms become interstate or state law by being codified in treaties or gelling into custom or by being ratified by state law or being used by an authoritative court.[628] However, in the latter instance that I propose here, the use of soft norms in

[627] For example, see Sara Joseph & Joanna Kyriakakis, "From Soft Law to Hard Law in Business and Human Rights and the Challenge of Corporate Power" 36:2 Leiden Journal of International Law 335–361; Barnali Choudhury, "Hardening Soft Law Initiatives in Business and Human Rights" in Jean J du Plessis & Chee Keong Low, eds, *Corporate Governance Codes for the 21st Century: International Perspectives and Critical Analyses* (Springer, 2017); Chiara Macchi & Clair Bright, "Hardening Soft Law: The Implementation of Human Rights Due Diligence Requirements in Domestic Legislation" in Nicole Lazzerini, Laura Magi & Deborah Russo, eds, *Legal Sources in Business and Human Rights: Evolving Dynamics in International and European Law* (218-247: Brill | Nijhoff, 2020).

[628] The hardening process can be done in different ways within States' own legal orders. Most importantly, soft norms could be ratified by state law when a national legislative permits incorporation by reference of soft-law norms into its own regulations as those soft-law norms change and without further need for further law-making by the State (this is known as ambulatory incorporation by reference). As pointed out in conversation by Professor Scott, section 18.1 of the federal *Statutory Instruments Act* (R.S.C., 1985, c. S-22) in Canada indicates that "the power to make a regulation includes the power to incorporate in it by reference a document—or a part of a document—as it exists on a particular date *or as it is amended from time to time*," *Instruments Act (R.S.C., 1985, c. S-22)*, online: <https://laws-lois.justice.gc.ca/PDF/S-22.pdf>. (emphasis added) This means that a federal statutory instrument may not only incorporate a document produced by Transnational Industry Association X but also incorporate the amendments to

international tribunals testifies to their ongoing existence as relevant rules external to the a given IIA, whereby they do not become state or interstate law by that use. This approach seems more in keeping with both the reality of the transnational globalized economy and the legitimate expectations of multiple actors acting within and affected by that economy. These norms, in their current form, are rules of law that are institutionalized out of constant interactions among States and non-state actors and are legitimized enough to create a sense of obligation among their objects, without going through incorporation or delegation processes of national statutory law or international treaty law.

Within the traditional state-centric framework of public international law, the factual element (state practice) and psychological element (*opinio juris*), which are expressed in the ICJ's Statute formula as "general practice" and "accepted as law," constitute the two defining elements of customary international law. However, the proliferation of non-state actors and the emergence of new legal norms have changed the normative landscape within which the traditional definition of customary international law has been operational for at least a quarter-century[629]—to the extent that transnational law norms, which I seek to examine in terms of their application in ISDS tribunals, are considered as "an adequate substitute for the defining elements of traditional customary law, *consuetudo* (practice and use) and *opinio necessitatis* (recognition of the norm's binding character)."[630] In this context, the recognition of self-regulated norms (soft law) in the form of transnationalized customary international law requires elaborated explanation on two integral elements:

- Why should non-state actors be considered to have authoritative lawmaking powers at the transnational level?

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that document by Transnational Industry Association X. In addition, soft norms could also become hard law when a court turns, for instance, business custom into an authoritative court-enforced meaning for terms in contracts and commercial disputes. See Kernaghan Webb, "The Law and Voluntary Codes: Examining the 'Tangled Web'" in Kernaghan Webb, ed, *Voluntary Codes: Private Governance, the Public Interest and Innovation* (Carleton University, 2004) 97.

[629] Craig M Scott, "Translating Torture into Transnational Tort: Conceptual Divides in the Debate on Corporate Accountability for Human Rights Harms" in Craig M Scott, ed, *Torture as Tort: Comparative Perspectives on the Development of Transnational Human Rights Litigation* (Oxford: Portland: Hart Publishing, 2001) 45; Craig M Scott & Robert Wai, "Transnational Governance of Corporate Conduct through the Migration of Human Rights Norms: The Potential of Transnational "Private" Litigation" in Christina Joerges, Inger-Johanne Sand & Gunther Teubner, eds, *Transnational Governance and Constitutionalism* (Oxford: Portland: Hart Publishing, 2004) 287.

[630] Calliess & Zumbansen, *supra* note 554 at 145.

- How can the legitimacy of non-state-based norms (with its implications for legal obligation) be recognized through different ways other than state consent?

To offer a convincing approach for addressing these questions, in the next section, I use a *legal pluralism* perspective that engages with transnationalized customary international law from a different knowledge paradigm than the one that classically tries to confine law to a state-centric framework.[631] Equipping ourselves with legal pluralism, in this way, would then pave the path toward my theoretical analysis of how law norms are institutionalized (by engaging with the hybrid theory) and my discussion of how transnational norms are legitimized (by involving the interactional theory) to consider them as transnationalized customary international law.

3.3 Global Legal Pluralism

> "The most appropriate analysis of the relations of legal systems is pluralistic rather than monistic, and interactive rather than hierarchical."[632]

The proliferation of official and unofficial, hard and soft norms at the transnational level "speaks to the need of adopting a sociologically and theoretically informed perspective rather than dismissing such developments as contrary to the perception of the state as exclusive author of law."[633] To build a sufficiently capacious understanding of the transnational lawmaking process, ideas around global legal pluralism have been developed within sociolegal scholarship to study and assess multiple normativities present in today's transnational order and the complex interactions between them. Sociolegal scholars have established global legal pluralism to explain the institutional and normative aspects of a transnational law comprised of multiple authorities[634] and faced with multiplying instances of transnational non-state lawmaking activity.[635]

Global legal pluralism is not as new as it is sometimes made out to be. Pluralism as a frame of reference in the encounter of societies, including of course colonial encounters, was initially

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[631] Paul Schiff Berman, "The Evolution of Global Legal Pluralism" in Roger Cotterrell & Maksymilian Del Mar, eds, *Authority in Transnational Legal Theory: Theorising Across Disciplines* (Cheltenham, UK: Edward Elgar, 2016); Fischer-Lescano & Teubner, *supra* note 307.
[632] Grant McCracken, *The Long Interview* (SAGE, 1988) at 256.
[633] Calliess & Zumbansen, *supra* note 554 at 110.
[634] Brummer, *supra* note 577.
[635] Berman, *supra* note 631.

discussed two centuries ago by Maine. He confronted the centrality of States' lawmaking power and interrogated the boundaries between public and private, formal and informal, and national and international—albeit without necessarily organizing the discussions into these tensions or pairings.[636] Contrary to the traditional legal paradigm focusing on the nation-state as a sole lawmaking power, legal pluralism regards diverse ways of private rulemaking through social communities across, beyond, or through States. Sociolegal scholars, such as Berger, unlike the state-positivistic lawmaking approach, "acknowledge that the formation of the law is not an exclusive governmental (domestic law) or inter-state (international law) prerogative and that legal theory must not be trapped within the traditional 2x2 matrix created by the dualities of 'public/private' and 'domestic/international'."[637] They also look into "a paradigm shift in the legal theory" in order to preserve spaces for productive lawmaking interaction among diverse and functionally differentiated social communities in a globalized context.[638]

To elaborate on the concept of social communities in a globalized context, Krisch evaluates the institutional aspect of transnational governance by suggesting the concept of "liquid authority" that loosens the boundaries of authority in contemporary discourses around international and transnational law. The model is based on a contrast between two ways of thinking about governance: solid and liquid. To think solidly, he writes, is to look for and see "commands and binding rules issued by an identifiable governor (or governing institution) over those subject to his or her rule."[639] Solidity here is a broader frame of hierarchies and clear demarcations between the governing and the governed binding powers, and the creation of formal obligations. Framing authority in a solid shape reproduces the top-down lawmaking process while ignoring soft norms that resemble the structures of transnational governance and risking relegating them to a sphere of lesser importance. By contrast, under the liquid frame, more dynamic authority structures can

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[636] The nineteenth-century evolutionism in the legal theory set initially by Maine and nurtured with the publication of Ancient Law. Henry Sumner Maine with the collaboration of Harvard University, *Ancient Law: Its Connection with the Early History of Society, and Its Relation to Modern Ideas* (London, John Murray, 1861). Maine sets the set the stage for anthropologists and sociologists like Durkheim, Morgan, Sorokin, Zimmerman and Max Weber who reconstructed their typologies of society on the approach and method of Maine, David M Trubek, "Max Weber on Law and the Rise of Capitalism" (1972) *Wisconsin Law Review* 720–753.
[637] Klaus Peter Berger, "History & Modern Evolution of Transnational Commercial Law" (2002) Trans-Lex Law Research para 59.
[638] Peer Zumbansen, "Transnational Legal Pluralism" (2010) 1:2 Transnational Legal Theory 141–189 at 151.
[639] Krisch, *supra* note 563 at 28.

be seen with multiple actors who occupy positions of authority with varying degrees of stability and consolidation. Reconceiving authority in the liquid way captures a broader part of communal interactions/practices in global governance thereby authority emerges beyond state sovereignty.

Roughan furthers the discussion by focusing on the legitimacy aspect of transnational governance. She notes that it is not sufficient for sociologists of law and theorists of legal pluralism to gloss over the details of the concepts they rely upon to distinguish legal norms from social norms, instead of explaining normative concerns about law's legitimacy. She starts her argument by criticizing the idea that the traditional (state-centric) conception of authority is divided into two categories: authority is treated as either a social power (to get other people to do what the authority demands) or a normative power (to impose obligations and change the reasons that apply to a subject). Roughan offers a two-step argument to bridge this conceptual divide of authority, either as a normative power replete with obligations and constituted by rules or as a social power dependent on *de facto* obedience and constituted by acceptance of collective subjects. First, she "insists upon the mutual dependence of the normative and sociological accounts, driven by a relationship of interdependence and captured in the explanation of authority as a 'normative-social practice'."[640] Second, she explains a conception of authority as relative normative power: "relative authority [that] illuminates both the social and the normative aspects of authority through an examination of the implications of plurality of authority in the transnational and non-state context."[641] The interdependence of normative and sociological aspects of authority can be seen in transnational governance, revealing both facts and reasons that generate relativity between authorities.[642] Therefore, conceiving authority in a transnational

[640] Nicole Roughan, "From Authority to Authorities: Bridging the Social/Normative Divide" in Roger Cotterrell & Maksymilian Del Mar, eds, *Authority in Transnational Legal Theory: Theorising Across Disciplines* (Northampton, MA: Edward Elgar Publication, 2016) at 282.
[641] *Ibid*.
[642] Instead of seeing supreme authority as a necessary precondition to law, Roughan offers a model of relative authorities that must "cooperate, coordinate, or tolerate one another if they are to have legitimacy", Nicole Roughan, *Authorities: Conflicts, Cooperation, and Transnational Legal Theory* (Oxford: Oxford University Press, 2013) at 8. The Roughan approach has parallels to the legal-pluralist transnational law theory of Keith Culver and Michael Giudice in their two books, Keith Culver & Michael Giudice, "Introduction" in *Legality's Borders: An Essay in General Jurisprudence* (New York: Oxford University Press, 2010) and Keith Culver & Michael Giudice, *The Unsteady State: General Jurisprudence for Dynamic Social Phenomena* (Cambridge: Cambridge University Press, 2017) in which they make out the case for understanding legality in terms of the interaction between legal institutions where patterns of intense mutual reference amongst the legal institutions generate complex forms of legality well beyond that of the "law-state" and of classically conceived public international (interstate) law.

context requires both a clear account of normative authority—its reason-giving and reason-dependent character—and social authority—its dependence upon the fact of people accepting and recognizing actual authorities. In this context, the legitimacy of transnational norms is tied to the distinctive characteristic of recognition or acceptance by the relevant social community or communities whose members are addressees or subjects of claimed legal norms—rather than to legitimacy indicators such as capacity to exact obedience through monopolization of coercive mechanisms or on theories of persuasion that fuse law with high ideals of deliberative reason and the like.[643]

For well over half a century, one school of international law has departed from state-centric positivism without veering into natural law as the only alternative, and theorized an account that, as with Roughan, sought to intermediate normativity and sociology. To examine the complexities of international lawmaking through the lens of overlapping, normative communities, the New Haven School of International Law has long criticized state-positivist understandings of international law, which they identified not as a set of formal rules but rather as a process of authoritative and controlling decision-making.[644] Within this decision-making process, McDougal and Lasswell write, "our chief interest is in the legal process, by which we mean the making of authoritative and controlling decisions."[645] They explain international lawmaking as a complex, decentralized, and diverse process, a loosely stitched patchwork of multiple norm-generating communities rather than a predictably centralized process let alone a state-centered centralized process. In 1981, Reisman argued that the New Haven School viewed international law not just as a series of written and implied agreements but as a "process of communication," comprising three communicative streams: "policy content, authority signal and control intention."[646] This communication model "liberates the inquirer from the … distorting model of positivism, which holds that law is made by the legislature," in favor of the notion that "any communication between elites and politically relevant groups which shapes wide expectations

[643] Roughan, *supra* note 640.
[644] Koh, *supra* note 561.
[645] Myres S McDougal & Harold D Lasswell, "The Identification and Appraisal of Diverse Systems of Public Order" (1959) 53:1 American Journal of International Law at 9.
[646] W. Michael Reisman, "International Lawmaking: A Process of Communication" (1981) 75 American Society of International Law Proceedings at 113.

about appropriate future behavior must be considered as functional lawmaking."[647] In their joint publication, "The World Constitutive Process of Authoritative Decision," McDougal, Lasswell, and Reisman explain international lawmaking as a participatory process that is driven by a diverse community of nation-states and transnational actors.[648] In their approach, non-state actors do not merely influence State-driven lawmaking processes but constitute such processes and make law themselves.

Being influenced by the New Haven School having done her PhD work at Yale with McDougall, Rosalyn Higgins analyzes the individual's status—subject or object—in the international legal system and who seeks to balance or reconcile its own private interests with the interests of State. She notes "it is not particularly helpful, either intellectually or operationally, to rely on the subject-object dichotomy that runs through so much of the writings [on public international law]."[649] Instead, international law should be seen as a decision-making process. She notes that "international law is a process, a system of authoritative decision-making. It is not just the neutral application of rules."[650] Within this dynamic and not static process, "there are a variety of participants, making claims across state lines, with the object of maximizing various values."[651] To explain how participants will promote their claims by a variety of techniques, ranging from force to diplomacy and public persuasion, Higgins initially discusses how General Assembly resolutions contribute to the development of customary international law and then expands her discussion to explain the issue of the accountability of international organizations for harm to third parties.

Lung-Chu Chen's *An Introduction to Contemporary International Law: A Policy-Oriented Perspective* is another important work that seeks to convince readers that individuals are active participants in the international decision-making process in general and customary law

[647] *Ibid* at 107.
[648] Myres S McDougal, Harold D Lasswell & W. Micheal Reisman, "The World Constitutive Process of Authoritative Decision" (1967) 19 Journal of Legal Education 253.
[649] Rosalyn Higgins, "Conceptual Thinking about the Individual in International Law" (1978) 4:1 British Journal of International Studies 1–19 at 5.
[650] Higgins, *supra* note 413 at 276.
[651] Higgins, *supra* note 649 at 5.

formation.[652] In this book, Chen says that in the current structure of international law, even within interstate treaties "individuals and private groups are given increased, though still limited, access to arenas of transnational authority to bring complaints about human rights deprivations against even their governments."[653] Concerning customary law formation, he notes that "[u]nder the concept of 'custom' that creates law through widely congruent patterns of peoples' behavior and other communications, individuals and their private associations have always participated in the prescribing [i.e. lawmaking] function."[654] In this statement, Chen deviates from the traditional approach of customary law and undertakes a more realistic assessment of how individuals play a role in the decision functions of (as New Haven School special terminology has it) intelligence, promotion, invocation, and appraisal. As an adherent to the New Haven School, Chen like Higgins goes beyond the subject-object dichotomy in international law and expands the domain of international subjects to include individuals and, indeed, "actors" (in international or transnational relations) in preference to the language of "subjects" (of international law).

One step further, Paust takes the position—thirty years ago—that individuals have a long-recognized role in customary law formation, and they are acknowledged already in customary law doctrine. In this view, there is "no single set of participants…Like all human law, [customary law] is full of human choice and rich in individual and group participation."[655] He believes that the subjective element of customary law is to be gathered from patterns of generally shared legal expectations among humankind, not merely among nation-states. This belief is well articulated in "Customary International Law: Its Nature, Sources and Status as Law of the United States" that says:

> The expectations of all human beings ("mankind", "the world", "the people") are not only relevant [to customary law] but they also provide the ultimate criterial referent. Indeed, no other ultimate referent would be realistic, since all human beings recognizably participate in such a process of acceptance and the shaping of attitudes whether or not such participation is actually recognized by each individual or is as effective as it might otherwise be (e.g., even if apathetic "inaction" is the form of participation for some, a form that simply allows others a more significant role) [footnote omitted]. It is this

[652] Lung-chu Chen, *An Introduction to Contemporary International Law: A Policy-Oriented Perspective* (New York: Oxford University Press, 1989).
[653] *Ibid* at 80.
[654] Ibid.
[655] Jordan J Paust, "The Complex Nature, Sources and Evidences of Customary Human Rights" (1995) 25 Georgia Journal of International and Comparative Law 147 at 147.

> ultimate referent, moreover, that provides customary law with a built-in basis for its own general efficacy, resting as it does on actual patterns of generally shared legal expectation, and with a claim to being the most democratic form of international law.[656]

This line of theoretical argument is evident in the decisions of *Urbaser* and *Nevsun* whereby rules of international law create causes of action against non-state actors (private corporations)—before a transnational tribunal in one instance and before national courts in the other. The ruling in the *Urbaser* case imposed a human rights liability on investors, considered investors to have a sort of transnational legal personality in international law according to which they were not just beneficiaries of rights owed by States, but holders of obligations owed to human rights beneficiaries, and obliged them to uphold international law including human rights. The tribunal explained that "a principle may be invoked in this regard according to which corporations are by nature not able to be subjects of international law and therefore not capable of holding obligations as if they would be participants in the State-to-State relations governed by international law. While such principle had its importance in the past, it has lost its impact and relevance in similar terms and conditions as this applies to individuals."[657] It was further added that the most favored treatment clause in the BIT shows that the state parties have already accepted that investors are entitled to invoke rights resulting from international law—and thus had subjecthood or personality at least to the rights-holding extent: "If the BIT therefore is not based on a corporation's incapacity of holding rights under international law, it cannot be admitted that it would reject by necessity any idea that a foreign investor company could not be subject to international law obligations."[658] The tribunal then moved to personality in the sense of the holding of obligations not just rights by noting that the crucial importance of corporate social responsibility standards and their acceptance within the domain of international law reveal that "it can no longer be admitted that companies operating internationally are immune from becoming subjects of international law."[659] The investment tribunal concluded that corporations are subjects of international law and then rejected the claimant's contention that guaranteeing the human right to water is a duty that may be born solely by the State, and never borne also by private companies

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[656] *Ibid* at 62.
[657] *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, *supra* note 3 para 1193.
[658] *Ibid* para 1194.
[659] *Ibid* para 1195.

like themselves—even as, on the facts of the case, the tribunal did not find the kind of obligations placed on corporations (essentially, negative obligations not to directly interfere with others' rights) had been breached.[660]

Similarly, in the *Nevsun* case, the Court majority explained that "modern international human rights law [is] the phoenix that rose from the ashes of World War II and declared global war on human rights abuses. [Thus,] its mandate was to prevent breaches of internationally accepted norms."[661] The Court went on to speak in Roughan-like terms (recall her conception of "authority as a 'normative-social practice'"), stating "[t]hose norms were not meant to be theoretical aspirations or legal luxuries, but *moral imperatives and legal necessities*. Conduct that undermined the norms was to be identified and addressed."[662]

The Court further explained that although States used to be the main subjects of international law, "the past 70 years have seen a proliferation of human rights law that transformed international law and made the individual an integral part of this legal domain, reflected in the creation of a complex network of conventions and normative instruments intended to protect human rights and ensure compliance with those rights. The rapid emergence of human rights signified a revolutionary shift in international law to a human-centric conception of global order."[663] The result of these developments, for the Court, is that international human rights norms must be applied to private actors. The Court accordingly rejected Nevsun's position that it is immune from the application of customary international law because it is a corporation. It noted that norms of customary international law, except those norms governing treaty making and those that are otherwise of a strictly interstate character, prohibit conduct regardless of whether the perpetrator is a state or a corporation.[664] The court referred to and approved Dodge's observation

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[660] See Chapter 1 for the comprehensive reasonings of the ISDS tribunal on the direct liability of foreign investors under international law.
[661] *Nevsun Resources Ltd. v. Araya,* Supreme Court of Canada, Case No. 37919, Judgment 28 February 2020, *supra* note 542 para 1.
[662] *Ibid* para 1 (emphasis added).
[663] *Ibid* para 108.
[664] Harold Hongju Koh, "Separating Myth from Reality about Corporate Responsibility Litigation" (2004) 7:2 Journal of International Economic Law 263–274.

that "[i]nternational law … does not contain general norms of liability or non-liability applicable to categories of actors,"[665] and decided "there is no longer any tenable basis for restricting the application of customary international law to relations between states."[666] It then concluded that it is not "plain and obvious" that corporations today enjoy a blanket exclusion under customary international law and thus are excluded from direct liability for their violations of customary international law—and thereby rejected the company's motion to have the customary international law claim against it (for violations of forced labour, slavery, torture, and other norms) dismissed on the basis of no reasonable cause of action.[667]

The above-mentioned theoretical explanations and doctrinal developments confirm the pluralistic lawmaking approach that "we live in a world of hybrid legal spaces, where multiple normative regimes may govern (or at least strongly influence) our activities and where authority tends to be relative, not absolute."[668] It also elaborates that "[s]ocially constructed rules, principles, norms of behavior, and shared beliefs provide states, individuals, and other actors with understandings of what is important or valuable and what are effective and/or legitimate means of obtaining those valued goods."[669] However, these arguments mainly focus abstractly on lawmaking beyond (or alongside) state power and lack concrete accounts of how multiple authorities are institutionalized in relation to each other and how legitimacy is conferred upon transnational soft law norms.

To understand the legal status of transnational self-regulated norms for the sake of knowing whether they could be treated as *applicable* law in ISDS tribunals, not only the contents of the norms and norm-generating processes of various actors should be analyzed but also the legitimacy of their being treated as rules of law must be studied. On that basis, I will examine the institutional and normative aspects of transnational self-regulated norms through the lenses of the

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[665] William S Dodge, "Corporate Liability Under Customary International Law" (2012) 43 Georgetown Journal of International Law 1045 at 1046.
[666] *Nevsun Resources Ltd. v. Araya,* Supreme Court of Canada, Case No. 37919, Judgment 28 February 2020, *supra* note 542 para 107.
[667] *Ibid* para 113.
[668] Paul Schiff Berman, "Understanding Global Legal Pluralism: From Local to Global, from Descriptive to Normative" in Paul Schiff Berman, ed, *The Oxford Handbook of Global Legal Pluralism* (Oxford Handbooks Online, 2020) at 5.
[669] Martha Finnemore, *National Interests in International Society* (Ithaca and London: Cornell University Press, 1996) at 15.

"hybrid theory" and the "interactional theory." The hybrid theory depicts the transnational regulatory framework as occupied by hybrid lawmaking powers in contrast to state-monopolized powers, particularly in the face of growing transnational and non-state claims to normative authority. It also explains relational networks among the contested transnational lawmaking powers. The interactional theory proposes communal interaction among diverse actors and day-to-day perceptions of efficacy as integral elements for granting legitimacy qua law to transnational norms, rather than the traditional model of confirming formal legality of claimed customary international law rules by combining evidence of individual States' *opinio juris* into a conclusion of sufficient interstate consensus.

3.4 The Hybrid Theory

The hybrid theory draws on the legal pluralism insight to discuss the *institutional aspect* of the formation of transnational law: who are the lawmaking powers of transnational law and how does the answer to that affect or determine the content of law where multiple institutions have a role? The hybrid theory cannot be located in first use by any specific author but emerged as a term that a range of scholars has increasingly applied to explain globalized economic governance dealing with the proliferation of non-state lawmaking actors and non-state-based norms.

A well-argued statement is put forward by Kreide, who reveals a much-needed appreciation of the hybrid regulatory regimes for transnational law, promulgated by public and private norm-producing entities.[670] Kreide notes that the parallel processes of the growing importance of non-state actors' lawmaking role and the continuing formalization of state-based law amount to echoing new trends of the hybrid institutional structure of transnational law. She observes "[p]olitical power and the market enter into an alliance that, without being based on a legal acquisition of power, cuts across the functional differentiation between right and wrong, government and opposition, haves and have-nots."[671] Koh also argues transnational law "denotes a hybrid body of law that transcends old dichotomies between international and domestic law and

[670] See Robert E Scott & Paul B Stephan, *The Limits of Leviathan. Contract Theory and the Enforcement of International Law* (Cambridge: Cambridge University Press, 2006).
[671] Regina Kreide, "The Ambivalence of Juridification. On Legitimate Governance in the International Context" (2009) 2 Global Justice: Theory Practice Rhetoric at 22.

between public and private law."[672] Instead, as discussed by Berman, transnational norms are institutionalized through the lens of communal interactions among hybrid actors, including "a wide range of entities, from official transnational and international regulatory and adjudicative bodies to non-governmental quasi-legal tribunals to private standard-setting or regulatory organisations."[673]

Furthermore, Macaulay offers a deeper understanding of transnational governance's institutional dimensions that are neither purely private nor public. He notes that when we want to study law at the transnational level, "sharp lines cannot be drawn between the formal and the informal or between the public and the private."[674] In "Private Government," Macaulay explains that there is no division between public and private governance, and much of the lawmaking and dispute resolution in any society is carried out by private governments influenced directly or indirectly by public ones:

> Much of what we call governing is done by groups that are not part of the institutions established by federal and state constitutions. If governing involves making rules, interpreting them, applying them to specific cases, and sanctioning violations, some or all of this is done by such different clusters of people such as the Mafia, the National Collegiate Association, the American Arbitration Association, those who run large shopping centers, neighborhood associations, and even the regulars at Smokey's tavern. It may be necessary to draw a sharp line between public and private governments such as these in order to think about law, but in reality, there is no such division. To the contrary, one finds instead interpenetration, overlapping jurisdictions, and opportunities for both harmony and conflict among public and private governments.[675]

By turning to the hybrid theory, which emphasizes the complex communal law-generating interactions between State (public) and non-state (private) actors and the hybrid nature of the substantive norms that result,[676] the institutional aspect of transnational law should be evaluated with respect to the relationship between States and non-state actors: are they adversarial or complementary, or a mixture dependent on context? To evaluate the interaction between States

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[672] Koh, *supra* note 561 at 114.
[673] Paul Schiff Berman, "Global Legal Pluralism" (2007) 80 Southern California Law Review at 325.
[674] Stewart Macaulay, "The New versus the Old Legal Realism: Things Ain't What They Used to Be" (2005) 2 Wisconsin Law Review 365 at 399.
[675] Stewart Macaulay, "Private Government" in Leon Lispon & Stanton Wheeler, eds, *Law and the Social Sciences* (Washington, D.C.: Russell Sage, 1986) at 445.
[676] Lisa Bernstein, "Opting out of the Legal System: Extralegal Contractual Relations in the Diamond Industry" (1992) 21 Journal of Legal Studies 115.

and non-state powers at the transnational level and examine whether they are interacting in an adversarial or complementary mode, I engage with Calliess and Zumbansen who point to the hybrid character of transnational law, substantively and procedurally, between or beyond the public/private divide.

3.4.1 Substantive Aspect of Transnational Law

Calliess and Zumbansen take a functionalist perspective that says both the authors and content of transnational law should be categorized as a hybrid with regard to the traditional distinction between public and private law spheres. Instead of assuming a world in which we would be able to draw a neatly cut distinction between rules created by States or non-state actors, Calliess and Zumbansen challenge the exclusionary basis on which state-centered law is shielded from the outside and illustrate the tension between public and private actors in transnational governance. They expand the hybrid theory that suggests how both States and non-state entities could mutually "cooperate" in creating transnational rules that perform a hybrid function of maintaining both efficiency and justice in the market economy:

> [R]ather than assuming a world in which we would be able to draw a neatly cut distinction between a public and a private sphere of norm-making, we suggest pushing the qualifications of co-ordinative and regulatory that have been associated, respectively, with private and public law, further towards a critical study of how the changing ideas of coordination and regulation influence our understanding of public and private with regard to emerging actors and forms of legal norm-creation.[677]

In their *Rough Consensus and Running Code: A Theory of Transnational Private Law*, Calliess and Zumbansen note that the hybrid model of lawmaking at the transnational level can not only engage States and non-state actors but also combine public law's value for promoting justice and private law's value for increasing efficiency at the transnational level.[678] They develop their hybrid theory initially by highlighting the contestation associated with "new governance" within national lawmaking orders and engaging with the transformation of public/private distinction at the national level. Against this national depiction, they then move towards the battle over the institutional dimension of transnational law and characterize the nature of lawmaking in the

[677] Calliess & Zumbansen, *supra* note 554 at 100.
[678] See Calliess & Zumbansen, *supra* note 554.

transnational realm by combining the co-ordinative and regulatory functions as well as the substantive and procedural aspects of transnational law.

At the national level, Calliess and Zumbansen note that the State at one time was singularly burdened with the task of minding the public good in a society composed of self-interested individuals (substantive dimension) and also was recognized as a distinct lawmaking actor representing the whole towards the rest of society (procedural dimension). On the *substantive* plane, national law is divided into private law and public law. In the former, the State oversees the relations between individuals and facilitates the cooperation of economic actors in markets; this can be called the *co-ordinative* function of law that deals with the market efficiency goal. Public law, on the other hand, would govern the state's activities in relation to individuals and regulate societal relations concerning public values; this is conceived as the *regulatory* function of law that concerns maintaining justice (non-efficiency goal) in the market. On the *procedural* plane, States are equipped with a monopoly on legitimate lawmaking, adjudication, and law enforcement. In this scenario whereby States have gradually been elevated to the status of the sole creator of binding norms, non-state-based norms are often uncomfortably depicted as soft law, mere guidelines or recommendations.[679] They may become relevant in the national legal system only indirectly through incorporation or delegation processes confirming state law's supremacy.[680]

However, the rapid transformation of public service delivery and the rise of public-private partnerships have challenged national law's substantive and procedural aspects. Regarding the substantive aspect, the blurring of spheres of competition/public law and contract/private law is mostly evident in national economic governance whereby rules governing market participants' relations (co-ordinative function with efficiency goal) and rules correcting market failures (regulatory function with justice goal) are intertwined.

[679] Alvarez, *supra* note 601.
[680] Ralf Micheals, "The Re-State-Ment of Non-State Law: The State, Choice of Law, and the Challenge from Global Legal Pluralism" (2005) 51 Wayne Law Review 1209.

3.4.2 Procedural Aspect of Transnational Law

Similarly, in the procedural aspect, in fields such as economic arbitration, States leave some space for private judges to issue arbitral awards that are then recognized and enforced by state courts. General principles of contract law are often referenced by arbitral tribunals, collected and formalized in the form of private codifications such as the International Institute for the Unification of Private Law (UNIDROIT) Principles of International Commercial Contracts. Beyond being part of private arbitration that state judiciaries recognize and enforce, States also explicitly use these privately-made principles to enact national law rules that complement the 1980 UN Convention on the Sale of International Goods (CSIG) as a public international law instrument.[681] This new depiction of economic governance testifies to a growing recognition that the modern State is not unilaterally intervening in societal affairs from an elevated position but must instead be conceived as just one (lawmaking) power among others. Another example to underline the intertwined nature of both the co-ordinative/regulatory and public/private functions of law in economic governance is that, although economic norms may be enforced through private litigation, their substantive orientation includes public values such as environmental protection. For example, the UNGC, though a non-state-based codification, incorporates public values like environmental protection by encouraging businesses worldwide to align their operations and strategies with ten widely accepted principles.[682] The UNGC embeds public values into corporate conduct by promoting sustainability, transparency, and accountability, thereby bridging the gap between private interests and global environmental concerns.

At the transnational level, troubles in dealing with the multipolar sources of norms in the domestic arena have been further exacerbated due both to the emergence of transnational corporations as integral participants and to the lack of centralized state sovereignty. In this regard, the critical understandings of "new governance," which imply a certain impossibility of upholding the distinction between the public/private law and also made a fast career in capturing the "cooperation" between States and non-state actors at the national level, open a window of opportunity to analyze the institutional aspect of transnational law. Therefore, regulatory

[681] Michael Joachim Bonell, "Unification of Law by Non-Legislative Means: The UNIDROIT Draft Principles of International Commercial Contracts" (1992) 40 American Journal of International Law 617.
[682] United Nations Global Compact (UNGC), *supra* note 5.

transformation at the national level motivates Calliess and Zumbansen to bring insights from this cooperative governance at the transnational level to understand new actors and new norms at that level.

Building on the discussion of the coordinative/regulatory functions and substantive/procedural dimensions, they discuss the hybrid nature of both norms' functions and norms' creators in transnational economic legal orders. As for the *substantive* line of inquiry into the nature and orientation of the norms governing transnational activities, they note "anything that can be recognized as transnational law, even if developed essentially by "private" actors such as traders in transnational commercial networks or corporations and corporate groups (as transnationally operating norms of corporate social responsibility), will have important public aspects "that go beyond a mere compromising of private interests in transnationally operating groups or networks."[683] Transnational private/commercial norms cannot be purely coordinated so as to be concerned with efficiency only. Instead, in the absence of a world State, such norms have to mutually deal with both the co-ordinative and regulatory aspects of global economic exchange. As a result, transnational law regimes in practice involve and combine both efficiency and justice functions. On the *procedural* plane, they "find a continuing and, by any measure, dramatic proliferation of norm-entrepreneurs, in other words of producers of guiding rules and in many cases binding norms," who are pressured to participate in existing law-making processes and to become autonomous authors of globally binding rules.[684]

However, one of the most radical limitations of the hybrid theory explaining the institutional dimension of transnational governance regime is its shortcoming in evaluating the legitimacy and binding quality (normative dimension) of self-regulated soft law norms. It thus raises substantial questions regarding which authorities will recognize the legitimacy of transnational norms and the process through which transnational norms acquire binding status. As it was revealed above and also declared by Cotterrell, in "What Is Transnational Law?," these questions are only unsystematically, somewhat inconclusively, and at times opaquely considered in Calliess and

[683] Cotterrell, *supra* note 598 at 509.

Zumbansen's hybrid theory, mostly in the discussion of the procedural aspect of transnational law.[685] To the extent that they make only a brief reference to Drobnig, who argues that the legitimacy of transnational norms arises not from *ratione imperii*—legitimacy based on the authority or power that issues the norm (e.g., a State or a sovereign entity)—but from *imperio rationis*—legitimacy based on the reasoned, inherent content of the norm itself, it means the normative force of such norms is derived not from the issuing authority but from their inherent rational and substantive content.[686] Calliess and Zumbansen also succinctly appraise, without further justifications, Fuller's "inner morality" of law,[687] which was based on a complex procedural-normative understanding of law for assessing the normative aspect of (hybrid) non-state-based norms.

The shortcomings of the hybrid theory in capturing the normative dimension of transnational norms are compounded by the inadequacies of conventional models that explain the relationship between public law and private ordering within the nation-state—namely, through mechanisms such as incorporation, deference, or delegation as expressions of state consent.[688] In national legal governance that "holds the state to be the relevant creator of binding norms, non-state norms are often uncomfortably depicted or dismissed as 'soft law', as mere guidelines or recommendations."[689] Transnational self-regulated norms will then be able to acquire legal status only within the frameworks of state consent as a category with subordinated status to state law supremacy.[690] However, this becomes problematic where authoritative acts of States are largely absent due to the erosion of a relatively solid institutional framework of state involvement in transnational lawmaking, which is instead driven to a great extent by transnational

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[685] Cotterrell, *supra* note 598 at 511.
[686] Ulrich Drobnig, "Ein Vertragsrecht für Europa'" in Peter-Christian Müller-Graff, Jürgen F Baur & Klaus J Hopt, eds, *Festschrift für Ernst Steindorff zum 70 Geburtstag am 13 März 1990* (Berlin/New York: Walter de Gruyter, 1990) 1141 publisher: RWS-Verlag. Although Calliess and Zumbansen point out the Drobnig's understanding of normative legitimacy based on the rational content of norms, they somehow criticized him by arguing that the sole focus on the content of the norms in question would provide little guidance for an understanding of their status or, arguably, their normative context.
[687] See Lon L Fuller, *The Morality of Law* (New Haven: Yale University Press, 1969).
[688] Micheals, *supra* note 680.
[689] Calliess & Zumbansen, *supra* note 554 at 109.
[690] Micheals, *supra* note 680. See also Janet Koven Levit, "Bottom-Up International Lawmaking: Reflections on the New Haven School of International Law" (2007) 32 Yale Journal of International Law 393 that explains private norms either lack legal status by being circumscribed as soft law, or they are transformed into legitimate hard law by authoritative acts of state consent.

corporations.[691] Therefore, to identify law from non-law and at the same time to acknowledge the legitimacy of transnational norms, in the next section, I engage with the *interactional theory* that aims to emphasize the importance of communal interactions among lawmaking powers as the crux of legitimacy rather than dictating legitimate norms hierarchically.

3.5 The Interactional Theory

> "Interactional framework reveals how legitimacy is built through broad participation in the construction and maintenance of legal regimes."[692]

Legitimacy is a crucial aspect of all legal norms because if a norm lacks legitimacy, its legal status will be challenged, reducing its binding quality as a matter of social practice. In the traditional lawmaking framework, legal norms would obtain legitimacy through state/interstate consent, either when they are created by state/interstate power or when they are incorporated by state power as a category with subordinated status in confirmation of the state/interstate law supremacy. However, in accordance with the pluralistic approach, expanding the scope of lawmaking authorities beyond States and explaining the bottom-up lawmaking process, the legitimacy of legal norms should be determined by looking for recognition by those who are subject to norms or who observe norms.[693] In this approach, what characterizes the foundation of law (its legality) is not formal actions of superior state authorities, applications by courts, and enforcement by centralized political power—at best, these actions produce law in form alone. For legality in deeper sense, one needs a theory of legitimacy. In broad terms, this dissertation accepts Franck's general understanding of the legitimacy of legal norms as following from their emergence from within "communal interaction" and the "perception of a rule as legitimate by those to whom it is addressed."[694] The more detailed fleshing out of what this means will, however, be centered on the work of Brunnée and Toope.

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[691] Calliess & Zumbansen, *supra* note 554 at 52.
[692] Brunnée & Toope, *supra* note 555 at 53.
[693] Cotterrell, *supra* note 586 at 263.
[694] Thomas M Franck, "Legitimacy in the International System" (1988) 82 American Journal of International Law 705 at 712.

Unlike the abstract philosophical theory of law's legitimacy upheld by Raz, in *The Authority of Law*,[695] in which central to the uniqueness of law is the formal nation-state-oriented mode of law that claims authority and supremacy over its subjects and legal systems, the notion of "communal interaction" focuses on social acceptance and a corresponding efficacy (notably, evidence of willing compliance without coercion) as indicators for legitimacy.[696] Berman likewise notices the great importance of communal interaction in the perception of legitimacy and notes law is supposed to "make aspirational judgments about the future, the power of which depends on whether the judgments accurately reflect evolving norms of the communities that must choose to obey them."[697] In his view, legitimacy is a matter of acceptance/recognition by members of the community within which legal norms are developed.[698] Lefkowitz further explains this acceptance, which depends in turn on whether members view a given norm as the correct extension of their historical practice of holding one another to account:

> [N]o actor has the power to unilaterally determine what the law is, and so how political power ought to be exercised. That power lies only with some community of agents whose shared understanding of what the law is, manifest in their use of it to hold themselves and one another accountable, settles that question.[699]

Legitimacy understood in this sense—as a general theory of law—resonates more particularly with the contemporary lawmaking process at the transnational level, whereby a superior lawmaking authority does not exist and, instead, diverse actors interact to develop legal norms. To operationalize this perception of legitimacy, I embrace the *interactional theory* that mostly evolved around notions of "communal interactions" (with its emphasis on mutual recognition) and of "bottom-up" approaches (with their emphasis on social acceptance) to examine the normative dimension of transnational law. In this section, the discussion of the interactional theory begins with lawmaking at the national level and then continues to the international level. This discussion explains how communal interaction among diverse lawmaking powers develops transnational norms whose legitimacy is recognized by those who both create the norms and are

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[695] Joseph Raz, *The Authority of Law*, second edn (United States, New York: Oxford University Press, 2009).
[696] Berman, *supra* note 631.
[697] Paul Schiff Berman, *Global Legal Pluralism: A Jurisprudence of Law Beyond Borders* (Cambridge: Cambridge University Press, 2012) at 213.
[698] Chris Thomas, "The Concept of Legitimacy and International Law" *LSE Legal Studies Working Paper*.
[699] David Lefkowitz, "Global Legal Pluralism and the Rule of Law" in Paul Schiff Berman, ed, *The Oxford Handbook of Global Legal Pluralism* (Oxford Handbooks Online, 2020) at 380.

subject to the norms. I should note here that although the interactional theory is primarily intended to discuss legitimacy at the domestic level and then at the (public, understood as interstate) international level, in my study, I will apply the interactional theory by extending Fuller, Brunnée, and Toope's insights in directions that allow it to be used to assess the legitimacy of (hybrid) non-state-based transnational norms. Given that their core assumptions about domestic and international law—namely, that law emerges through the interactions of diverse actors and that a sense of responsibility/fidelity arises when actors can reason with norms —align closely with those underpinning transnational law, interactional theories for legitimate lawmaking can be effectively extended to the transnational context.

The interactional theory was initially developed by Fuller and then extended by Brunnée and Toope to reveal "how legitimacy is built through broad participation in the construction and maintenance of legal regimes."[700] In *The Morality of Law*, Fuller introduces a process-oriented understanding of legitimacy and shows that the hierarchical manifestation associated with national law is neither necessary nor sufficient to endorse legitimacy even at the national level.[701] He notes that the legitimacy of state law depends "on effective interaction and cooperation between citizens and lawmaking and law-applying officials."[702] Brunnée and Toope, in *Legitimacy and Legality in International Law: An Interactional Account*, expand the interactional theory to explain the legitimacy of law at the international level. They argue that the legitimacy of international law does not lie either in formalism or in enforcement mechanisms.[703] Instead, they explain: "law is created and maintained through interaction. It is interaction that makes this relationship 'horizontal' and 'reciprocal', and is the core of 'legal' legitimacy."[704]

Beginning with Fuller's approach to the interactional theory, at the national level, he focuses on two key ideas: 1) the generation of legal norms through interaction among diverse actors and 2) the sense of responsibility (fidelity) to legal norms that arises only from the actors' ability to reason with norms. To explain the first idea, he contends that lawmaking requires upholding

[700] Brunnée & Toope, *supra* note 555 at 53.
[701] Fuller, *supra* note 687.
[702] *Ibid* at 194.
[703] Brunnée & Toope, *supra* note 555 at 53.
[704] *Ibid* at 54.

diversity in society[705] and dismisses the existence of hierarchical political authority.[706] Regarding the second idea and to organize social interactions among diverse actors, Fuller claims that lawmaking actors should reciprocally fulfill legal obligations and develop "fidelity" to legal norms if such norms meet eight "criteria of legality."[707]

Fuller notes that the lawmaking process is a continuing struggle of non-hierarchical but horizontal social interactions among governmental (State) and social (non-state) participants that generate fidelity to legal norms among them.[708] He views law as "the enterprise of subjecting human conduct to the governance of rules,"[709] which is not created by superior state power over others.[710] "Subjecting" in this view does not acknowledge the command-and-control model of legal effectiveness grounded in the enforcement power of sovereign States. Instead, he notes that no law is merely the imposition of authority and law depends for its existence "on effective interaction and cooperation between citizens and lawmaking and law-applying official."[711] Fuller explains law is a purposive process that is both shaped by human interaction and aimed at guiding that interaction in distinctive ways. It means law can be developed when actors reciprocally collaborate to build shared understandings as well as to uphold a practice of legality. Reciprocity creates relatively stable patterns of expectation from repeated social practice both amongst the governed and between the governed and the governing. It refers to the idea that "legal norms and authoritative directives can guide self-directed social interaction only if they are broadly congruent with the practices and patterns of interaction extant in the society generally."[712] Within this non-hierarchical, not defined by force, and mutually constructed

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[705] Similar reinterpretations of diverse autonomy are found in Jennifer Nedelsky, "Judgment, Diversity, and Relational Autonomy" in Ronald Beiner & Jennifer Nedelsky, eds, *Judgment, Imagination, and Politics: Themes from Kant and Arendt* (Lanham: Rowman & Littlefield, 2001) 103.
[706] For a similar argument, see Terry Nardin, "Legal Positivism as a Theory of International Society" in David R Mapel & Terry Nardin, eds, *International Society: Diverse Ethical Perspectives* (Princeton University Press, 1998).
[707] See also Kenneth Winston, "Three Models for the Study of Law" in Willem J Witteveen & Wibren van der Burg, eds, *Rediscovering Fuller: Essays on Implicit Law and Institutional Design* (Amsterdam University Press, 1999) at 69.
[708] Fuller, *supra* note 687 at 106.
[709] Lon L Fuller, *The Morality of Law* (New Haven: Yale University Press, 1969) at 106; See also Lon L Fuller, "American Legal Philosophy at Mid-Century" (1954) 6 Journal of Legal Education 457 at 467.
[710] Here Fuller dismisses the importance of coercion and enforcement in creating legal norms. This is one of the key elements distinguishing Fuller from American Legal Realists, whose interest in legal norms was largely limited to the enforcement capacity of States.
[711] Fuller, *supra* note 687 at 194.
[712] Gerald J Postema, "Implicit Law" in Willem J Witteveen & Wibren van der Burg, eds, *Rediscovering Fuller: Essays on Implicit Law and Institutional Design* (Amsterdam University Press, 1999) at 265.

conception of law, Fuller argues that what distinguishes law from other social norms has roots in certain conditions (criteria of legality) to allow human beings to pursue their purposes through law and for law to guide their actions and interactions. In this process, "the rule of law provides some normative grounds for thinking that citizens have an obligation to obey the law."[713] This obligation to obey is self-generated (fidelity) and is rooted in a sense of legitimacy gained primarily from upholding the eight criteria of legality.

In Fuller's view, law is mutually constructed when diverse participants effectively interact to build shared understandings through repeated social practices that are aimed at organizing (social) interactions among these participants, who are subject to law. However, although not all social actors have the same power to develop and maintain shared understandings, the interactional process takes major strides toward undercutting the ability of powerful actors to prefer and advance only the normative claims based on their own perceptions of self-interest. In order to become legal norms, such claims have to meet certain criteria of legality.[714] Laws must be **general (#1)**, specifying rules prohibiting or permitting behavior of certain kinds for the whole group of specific individuals, the constraint imposed on one is imposed on all.[715] Laws must also be widely **promulgated (#2)**, or publicly accessible. Publicity of laws ensures citizens know what the law requires. Laws should be **prospective (#3)**, identifying how individuals ought to behave in the future rather than prohibiting behavior that occurred in the past. Laws must be **clear (#4)**. Citizens should be able to identify what the laws prohibit, permit, or require. Laws must be **non-contradictory (#5)**, law should avoid contradiction and one law cannot prohibit what another law permits at the same time. Laws must be realistic and **not ask the impossible (#6)**. Laws should not be changed frequently; the demands laws make on citizens should remain relatively **constant (#7)**. Finally, there should be **congruence between what written statutes declare and how officials enforce those statutes (#8)**.[716] This means "the existence of duties

[713] Colleen Murphy, "Lon Fuller and the Moral Value of the Rule of Law" (2005) 24 Law and Philosophy 239 at 242.
[714] Fuller, *supra* note 687 at 39. Fuller has an extended discussion of each criterion from pp. 46–90.
[715] Fuller notes that this generality requirement is consistent with general injunctions on behavior being issued to specific individuals or groups. To meet the generality requirement, laws need not apply to the entire population.
[716] So, for example, congruence requires lawmakers to pass only laws that will be enforced and requires officials to enforce no more than is required by the laws. Judges should not interpret statutes based on their personal preferences and police should only arrest individuals they believe to have acted illegally.

depends partly on the behavior of others."[717] Citizens will not feel obliged to act in certain matters if no similar expectations apply with respect to those judging that person's behavior.

When lawmakers respect these eight criteria or principles, citizens can reason with the legal norms, form expectations about how others will act with respect to the legal norms, and reinforce the legal norms through reciprocal "practice of legality." These expectations are the basis for the legal duties that participants have towards one another. Indeed, they justify the belief that legal norms give citizens reasons to act or refrain from acting in certain ways. The outcome of this process is the possibility of generating "fidelity" to law among and legitimizing law in the eyes of participants who want to abide by the promulgated law.[718]

Within this conception of law, "the rule of law provides some normative grounds for thinking that citizens have a moral obligation to obey the law."[719] These normative grounds to create legitimate law depend on certain conditions: mutual interactions among diverse actors develop shared understandings; shared understandings are codified into legal norms; legal norms should meet the criteria of legality to develop legal duties; participants reciprocally fulfil legal duties; and reciprocal fulfillment of duties generates fidelity to law among participants. In this process, the legitimacy (the bindingness quality) of legal norms is "self-generated." It has roots mostly in the eight criteria of legality to generate fidelity to—feeling obliged to obey—legal norms.[720] Legal obligation is therefore conceptualized as internalized commitment and not as externally imposed duty. In other words, when the eight criteria of legality are met, law will generate fidelity in the persons to whom it is addressed, attract its adherence, become "self-binding," and be recognized as legitimate by subjects to it.

Contrarily, Fuller notes that when lawmakers fall far short of meeting the criteria of legality, the normative aspect of legal norms is fundamentally flawed, and they lack legitimacy to one degree or another (i.e. depending on how many of the criteria are unfulfilled and on the extent of non-

[717] Murphy, *supra* note 713 at 242.
[718] David Dyzenhaus, "Fuller's Novelty" in Wibren van der Burg & Willem J Witteveen, eds, *Rediscovering Fuller: Essays on Implicit Law and Institutional Design* (Amsterdam University Press, 1999) 97.
[719] Murphy, *supra* note 713 at 242.
[720] In this conception, there is no need to have centralized political order to enforce law, instead, citizens have a moral obligation to obey the law.

fulfilment). Thus, citizens start to feel resentment toward legal duties. Citizens feel resentment if the expectations are not clear, or are contradictory, or demanding the impossible. Citizens feel resentment if government officials unequally impose legal obligations only on certain groups and individuals, especially if governing elites, their friends, family and associates, and their influencers benefit most from the disparity. Citizens feel resentment if they cannot form reliable expectations due to frequent changes in law. Citizens feel resentment if officials pass retrospective legislation, and they do not know how the government expects them to behave in advance. Citizens feel resentment when officials expect them to fulfill certain duties, like obedience to law, despite the failure of government officials to fulfill their reciprocal duties. Then, citizens will no longer reciprocally fulfill legal norms and no longer develop fidelity to obey the dictates of the government.

Brunnée and Toope, who discuss the legitimacy of international law, start from the premise that the criteria of legality suggested by Fuller are largely uncontroversial as aspects of legitimate law. They argue that Fuller's eight criteria of legality are so important for understanding international law and capture the essence of the rule of law. By focusing on indicators of legality that are internal to law, Fuller's perspective provides them with a helpful lens to reflect on international law. But Brunnée and Toope's interactional theory carries additional insights for "explor[ing] the impact of international law on state conduct, and compliance."[721]

They provide a new perspective on Fuller's criterion of congruence to show that "in international society at least, congruence requires the substantial compliance of all participants in a legal system with not only the criteria, but also a continuing practice of legality."[722] By focusing on the concept of a legal obligation, which can contribute to "the important enterprise of distinguishing law from the morass of approaches to governance in which it threatens to disappear,"[723] Brunnée and Toope intend to explain the normative aspect of international law in the non-hierarchical legal system through five key points.[724] First, horizontality is an asset for, not a defect of, law.

[721] Brunnée & Toope, *supra* note 555 at 16.
[722] *Ibid*.
[723] Benedict Kingsbury, "International Law as Inter-Public Law" in Henry R Richardson & Melissa S Williams, eds, *NOMOS XLIX: Moral Universalism and Pluralism* (New York University Press, 2009) at 197.
[724] Brunnée & Toope, *supra* note 555 at 6.

Second, fidelity (a sense of obligation) to law, instead of enforcement, is the power that shapes human behavior. Third, diversity, rather than a centralized political order, would build a stronger global society. Fourth, a formalistic account of international law unduly confines our understanding of customary, treaty, and soft law. Fifth, legitimacy can be achieved in ways other than merely by state consent.

3.5.1 Horizontality Is an Asset for Law

To explain the horizontal nature of law (in all normative systems, even national law), social practices and mutual communal interactions among participants/actors/citizens would result in developing shared understandings. In turn, if these shared understandings are reinforced and codified by official agents' actions into legal norms that meet Fuller's criteria of legality, it becomes accordingly possible that social participants reciprocally fulfill legal duties and then generate fidelity to law that has been produced via the bottom-up process. The interactional view helps make sense of central features of the international legal system, which cannot be accommodated in theories predicated upon hierarchical projections of authority and thus is constantly challenged due to a lack of official sanctions against its violation. In this system wherein States are both subject to and makers of law and there is neither centralized enforcement power nor the political authority to generate legal norms, law is constructed horizontally through communal interactions among participants as its maintenance depends upon participants' practice of legality and fidelity to law.

In this view, although "power and force are salient to law, … they do not explain the sense of obligation that must exist in international society for legal enforcement to be possible and effective."[725] Nonetheless, in international law, which is not backed by common let alone centralized sanction, the fidelity to and the sense of bindingness of law are dependent upon certain criteria of legality and reciprocal fulfillment of legal duties and can also be undermined if law fails to be enforced. This statement does not intend to emphasize the importance of superior power to enforce law; however, it shows that fidelity to law might be damaged when law is seen to have no possibility of effect. It means laws that are "kept on the books as a kind of symbolic act, with the knowledge that they will not and cannot be enforced" lead to a sense of hypocrisy

[725] Murphy, *supra* note 713 at 242.

that undermines any commitment (sense of obligation) to the rule of law.[726] This is the lesson of Fuller's eighth criterion of legality: congruence between law and official action or, in the case of international law, congruence amongst the activities of a majority of international actors. When explicit rules are unrelated to how States and other international actors behave, fidelity to international law is destroyed.

3.5.2 A Sense of Obligation Is an Added Value of Law

Fidelity to international law and a sense of obligation, in different rationalist theories, often emerge through "reciprocity" as a series of transactions in which interests are exchanged for mutual advantages and predictability is shaped through interaction based on reciprocal interest. In *Problems and Process: International Law and How We Use It*, Higgins argues that international law ultimately functions on the basis of reciprocal obligations rooted in national interests: "As for the basis of obligation, reciprocity is a central element."[727] She explains that in international law "norms emerge either through express consent, or because there is no opposition … to obligations being imposed in the absence of such specific consent."[728] But implied consent extends even further than the idea of acquiescence ("because there is no opposition"). States undoubtedly come to perceive themselves as bound by norms that might be seen as even more "imposed" than those arising from silence that is taken as acquiescence—notably, norms that arise when they were not directly involved in the law-making process (the classic instance being new States being bound to custom that arose before they become states) or when they did not wish to accede to the evolution of a new legal norms but find themselves in a minority the specific proposal, yet do not seek to hold out against the norm's application through persistent objection.[729] The result is that individual-state and unanimous (i.e. all states) consent as the conceptual basis of customary international law has gradually been replaced by consensus as the

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[726] Fuller, *supra* note 687 at 153.
[727] Higgins, *supra* note 413 at 16.
[728] *Ibid*.
[729] I recognize there is a doctrinal debate on whether the principle of persistent objection allows an objecting State to stave off the application of a new norm to it indefinitely—in a manner directly analogous to a reservation to a treaty—or whether the principle ultimately means only that a State can delay the application of a norm through objection for a period that is reasonable for it to adjust its laws and practice to the new norm. The better view would seem to be the latter, but I will not weigh in on the matter further. See Ted L Stein, "The Approach of the Different Drummer: The Principle of the Persistent Objector in International Law" (1985) 26 Harvard International Law Journal 457.

basis of custom wherein reciprocity is understood as more diffuse than only the mutual exchange of specific material advantage and whereby, as Higgins expresses it, "that consensus comes about because states perceive a reciprocal advantage in cautioning self-restraint."[730]

However, in the interactional theory, "reciprocity is deeper than the exchange following from the calculation of material interests."[731] Reciprocity, as argued by Fuller, is defined in the context of the reciprocal fulfillment of duty that can be grounded in the desire to interact and to create sustained relationships.[732] In the national lawmaking process, if legal norms meet the criteria of legality, citizens will have the opportunity to reason with the norms and will reciprocally fulfill legal duties, whose existence depends partly on the behavior of others to generate fidelity to law. In this system, if the criteria of legality are neglected, citizens would miss the opportunity to reason with norms and have no desire to abide by the promulgated law, whereupon reciprocity fails and fidelity to law will not be generated.

In international society, this version of reciprocity is even more salient because States are both subjects and lawmakers, and the existence of international legal duties is extremely dependent on the behavior of other States. It means not all members of international society must be faithful to all international legal norms. Instead, reciprocity is created collectively to the extent that "interactional law can withstand individual defiance so long as a majority of actors works to uphold legality."[733] The collective nature of reciprocity explains why many developing States express their frustration over the existing rules of international law or over the evolution of international law and become skeptical as to why they should feel obliged to act in certain ways if no similar expectations apply with respect to those judging their behavior.[734] This resentment toward the creation of general international law is also analogous to resentment with the formation of a single treaty where the power imbalance between the parties eliminates real

[730] Higgins, *supra* note 413 at 16.
[731] Brunnée & Toope, *supra* note 555 at 38.
[732] This approach is influenced by the "logic of appropriateness" that engenders self-reflection and develops into a sense of legal obligation. See, James G March & Johan P Olsen, *Rediscovering Institutions* (New York: Free Press, 1989) at 23.
[733] Brunnée & Toope, *supra* note 555 at 40.
[734] Murphy, *supra* note 713 at 242.

opportunity for negotiations. In this process, although there is no mutual sense of duty, States have merely acted in the form of a treaty.

3.5.3 Diversity is Essential for a More Robust Global Society

The interactional theory explains lawmaking as a process dependent upon diverse participants in constructing and maintaining law. Fuller suggests that national legal norms are created only when diverse human beings interact in a community of practice to develop shared understandings of what they hope to achieve together and then generate fidelity to legal norms.[735] Citizens bring their diverse cultures and experiences to the table and know that they will not convince other actors of the desirability of a particular worldview. The "joint enterprise of members of a community of practice does not necessarily mean a common goal or vision."[736] But the community of practice provides a setting whereby diverse actors sustain their interactions, maintain their diversified autonomies, and develop shared understandings that later become legal norms that "shape how they perceive themselves and the world, how they form interests and set priorities, and how they make arguments or evaluate others' arguments."[737] This interactional process helps us to see how law is possible in societies where diverse moral/political ends are being pursued by citizens without the need to have centralized moral/political commitments. It would then turn into the gradual building up of global interaction, in Fuller's own view: "we should aspire to enlarge that community at every opportunity and to include within it ultimately, if we can all people of goodwill."[738]

At the international level, if diverse participants interact to build a shared understanding of an international issue and develop a relevant international legal norm, they would be able to reason from the legal norm to achieve their objectives and generate fidelity to law. Participants, at the international level, must extend beyond the sphere of States to include international organizations, NGOs, corporations, and informal intergovernmental and academic expert

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[735] See Fuller, *supra* note 687. In this book, Fuller articulates the internal morality of law as a set of eight principles that law must meet to be considered legitimate. What underpins this theory is the notion of law as a cooperative enterprise between the lawgiver and the subject. This cooperation presupposes a shared understanding and engagement, very much like what other scholars call a "community of practice."
[736] Emanuel Adler, *Communitarian International Relations: The Epistemic Foundations of International Relations* (London and New York: Routledge, 2005) at 22.
[737] Brunnée & Toope, *supra* note 555 at 65.
[738] Fuller, *supra* note 687 at 183.

networks who are actively engaged in the creation of shared understandings and the promotion of learning amongst States and other non-state actors.[739] It should be reiterated that shared understandings do not necessarily result in the development of a common goal or vision, but actors at least "must share collective understandings that tell [them] what they are doing and why."[740] Participants will then feel obliged to shape their interactions in light of the promulgated legal norm while preserving their autonomy to deepen shared understandings and gradually build up wider—including international or transnational—society. For example, as international participants communicate through a fundamental law, opportunities arise to deepen shared understandings around certain concrete issues, such as an environmental problem or a human rights concern, and even to cultivate normative convergence.

3.5.4 The Formalistic Account of International Law Is Not Inclusive

The interactional theory denies the heavy reliance on the formalistic account of legality, which see laws as only achieved through state consent, so it does not provide an accurate explanation of legal obligation and does not provide a convincing distinction between legal and social norms. In this approach, the formal model of lawmaking should not be mistaken for representing a legitimate legal norm: "although formal indicators provide useful indicia of the existence of binding rules and, of course, 'validity' on the terms of the system, they are not enough to identify 'law' because formality alone is not strong enough to generate fidelity."[741] Instead, the interactional theory distinguishes legal norms from social norms based on "a sense of obligation generated by fidelity to law."[742] Interactionism claims that the responsibilities imposed and the sense of obligation generated by legal norms are distinctive features that distinguish legal norms from social norms rather than the authoritative act of state consent. Through the lens of the interactional theory, compliance mechanisms and enforcement measures are not outcomes produced by or imposed on legal norms but are part of the continuing process of making legitimate law.

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[739] In some spheres, academic experts are central to the development of statements of applicable principles of law. For example, the Limburg Principles (1986) were developed by a group of international human rights experts in collaboration with the Urban Morgan Institute for Human Rights and the Faculty of Law at the University of Limburg (Netherlands): "The Limburg Principles on the Implementation of the International Covenant on Economic, Social and Cultural Rights," (1987) 9 Human rights quarterly 122-135.
[740] Adler, *supra* note 738 at 22.
[741] Brunnée & Toope, *supra* note 555 at 46.
[742] *Ibid* at 46.

At the international level, legal formalism pervades not just the theory but even the practical discourse of international law today—widespread is the exclusive confidence in traditional (i.e. the ICJ's Statute) sources of law as a means to define the existence of binding rules and to draw a bright line between law and non-law.[743] However, thinking about the creation of law in purely formal terms provides only limited guidance in analyzing how customary-based obligations are created in international society. In addition, although legal formalism provides useful information on the existence of binding rules, it undermines the importance of international norms developed by non-state actors (in their own interactions and/or in interaction with states) thar are capable of generating fidelity to law among the addressees of law. Here, the interactional account—an explanation combining interactions among diverse actors, shared understandings, the criteria of legality, and reciprocal practice of legality—explains how customary rules of international law are created through communal interactions and explains distinctive ways in which international law could be made through non-state-based legal norms, soft law.

Interactionalism is paramount in explaining the traditional formulation of customary law as arising from state practice plus *opinio juris*: there must be a widespread and sufficiently uniform practice of States, and States must engage in the practice out of a sense of legal obligation. The second requirement, *opinio juris,* is the central concept of customary international law as "it refers to the reason a state acts in accordance with a behavioral regularity, it is often described as the 'psychological' element of customary international law."[744] *Opinio juris* distinguishes state conduct (whether actions or omissions) done out of interest from conduct engaged in because of law. This requirement, which is defined as a "belief that [a] practice is rendered obligatory by the existence of a rule of law requiring it,"[745]challenges international lawyers with questions such as: How does State as an abstract entity believe something? How is this belief to be proved? Based on the formalist account of international law, lawyers typically address these questions by saying

[743] The idea that insists the validity of rules can only be measured by the consent of States, Martti Koskenniemi, "GENERAL PRINCIPLES: Reflexions on Constructivist Thinking in International Law" in *Sources of International Law* (Routledge, 2000).
[744] Eric A Posner & Jack L Goldsmith, *The Limits of International Law* (Oxford University Press, 2005) at 23.
[745] *North Sea Continental Shelf cases (Federal Republic of Germany/Denmark; Federal Republic of Germany/Netherlands),* International Court of Justice (ICJ), Judgment 20 February 1969, para 77.

that when a practice is sufficiently consistent and widespread enough among States, the *opinio juris* can be presumed.[746] However, if presumption in effect leads to no further inquiry, this makes *opinio juris* redundant with the state practice requirement, which, by assumption, is insufficient by itself to establish customary international law. There is also another conceptual hurdle: Posner and Goldsmith argue that *opinio juris*—the belief that a practice is legally obligatory—is conceptually problematic as it raises a circular logic issue, without clarifying the transformative process from a mere act to a legal obligation:

> there is no convincing explanation of the process by which a voluntary behavioral regularity transforms itself into a binding legal obligation. *Opinio juris* is described as the psychological component of customary international law because it refers to an attitude that states have toward a behavioral regularity. The idea of *opinio juris* is mysterious because the legal obligation is created by a state's belief in the existence of the legal obligation. *Opinio juris* is really a conclusion about a practice's status as international law; it does not explain how a widespread and uniform practice becomes law.[747]

Here, the interactional theory intends to explain that "a social norm, reflecting a shared understanding that meets the criteria of legality is upheld through practice that is congruent with the norm. This constitutes a 'practice of legality'. This enriched form of practice is what would traditionally have been called *opinio juris.*"[748] In this approach, customary law is not dependent upon state practice alone nor does it require *opinio juris* in the traditional sense of a belief that one's conduct is done to comply with law formed in advance of that conduct. Instead, customary legal norms become binding through interactional practice among diverse participants, which is rooted in the criteria of legality and grounds for continuing obligation. The conundrum Posner and Goldsmith pose does not disappear—where the conundrum is understood as the difficulty in determining the moment of formation of custom as the aggregate of conduct taking place with prior belief in legal status of a norm—but it shifts to a more objective analysis of the general pattern of behaviour of states for both the existence of the norm and determination of the critical date (when the norm gelled into law).

[746] Ian Brownlie, *Principles of Public International Law* (Clarendon Press Oxford, 1960) at 7.
[747] Posner & Goldsmith, *supra* note 744 at 24.
[748] Brunnée & Toope, *supra* note 555 at 47.

The interactional theory also provides a practical approach toward understanding soft law that cannot fit within formal sources of international law.[749] Through the lens of interactionalism, Brunnée and Toope argue that "'soft' norms may sometimes possess more obligatory force than norms derived from formal sources of law" backed by state consent.[750] When a non-state-based norm is rooted in shared understandings and adheres to the conditions of legality, it will generate fidelity to law, and international actors feel obliged to obey the norms. It is then hard to attack the bindingness of soft norms produced through interactional lawmaking. Chinkin further explains this point:

> While soft law may not be directly used to find a cause of action it has both a legitimising and a delegitimising direct effect: it is extremely difficult for a State that rejected some instrument of soft law to argue that behaviour in conformity with it by those who accepted it is illegitimate.[751]

In other words, although at first glance, soft law norms do not produce "causes of action" in order to be applied in adjudicative international decision-making only because soft norms are not included in Article 38 of the International Court of Justice statute, such norms can develop a sense of obligation among their addressees, which is the added value that constitutes law, in order to be used in the practical legal reasoning of courts.[752] Therefore, international lawyers should go beyond the formal manifestations of law and consider the nature and sources of communal obligation, which is a far more promising strategy for understanding how international law can emerge through interactional processes; neither a formal test for norms nor a hierarchy of norms can produce obligation.

3.5.5 Legitimacy Is Achieved through the Interactional Process

To specify a particular legal understanding of legitimacy, Fuller emphasizes that legitimacy is related to compliance and the capacity to generate fidelity to law. Instead of the authoritative act of state consent, "only when law is produced through the interactional framework we describe can it be said that the law is 'legitimate'."[753] The interactional theory reveals how legitimacy is

[749] Dupuy, *supra* note 576.
[750] Brunnée & Toope, *supra* note 555 at 51.
[751] Christine Chinkin, "The Challenge of Soft Law: Development and Change in International Law" (1989) 38 International and Comparative Law Quarterly 850 at 850.
[752] Brunnée & Toope, *supra* note 555 at 51.
[753] *Ibid* at 53.

built through the broad participation of diverse actors in the construction of shared understandings, through the satisfaction of criteria of legality, and the reciprocal fulfillment of legal duties. In other words, legitimacy is created horizontally when diverse participants reciprocally interact to create and maintain legal norms.

At the international level, although most international lawyers look to the formal sources of international law to explain legitimacy (thus conflating legitimacy with state-centered formal validity), the interactional theory emphasizes that "internal features of law [are] central to its power to promote commitment" and create legitimacy. For Brunnée and Toope, legitimacy is related to compliance in the sense that legitimate law has the capacity to generate fidelity to the rule of law and generate a sense of obligation to obey legal duties. Like Fuller, they too argue that when law is produced through the interactional process, it can be said that the law is "legitimate." It means that the first step in creating legitimate law is the emergence of widely shared understandings. If there are no shared understandings of diverse participants' common substantive ambitions, it will be difficult, if not impossible, to see the norms emerge as "law." The second step is that legal norms must substantially meet the criteria of legality. Those criteria are fundamental in producing norms that have the capacity to be called "law." The third step is that legal norms must be reciprocally fulfilled by participants through a continuing back-and-forth practice of legality. Brunnée and Toope highlight this three-step interactional process that "makes [lawmaking] relationship 'horizontal' and 'reciprocal', and is the core of 'legal' legitimacy."[754]

The legal legitimacy account of the interactional theory explains that for customary law to be created, a very particular kind of practice, which is inclusive practice and meets the criteria of legality, is required to make and sustain international legal norms. This process enables international lawyers to understand the reasons behind the weakness of many customary rules that have roots "not in the absence of enforcement or other attributes of 'hard' law, but in a legitimacy deficit resulting from limited participation in norm building and insufficient attention

[754] *Ibid* at 54.

to the requirements of legality."[755] To make the final point, Brunnée and Toope show that, through the interactional lawmaking process,

> even powerful states cannot simply impose "rules". If the legal rule is not grounded in shared understandings and if the criteria of legality are only weakly or imperfectly met, the rule will not generate fidelity, and it will not be employed in the reasoning of states as to appropriate behaviour. Conversely, even powerful states cannot escape existing rules that have generated widespread fidelity.[756]

To summarize these five statements, the interactional theory explains that the legitimacy of legal norms is not hierarchically inferred from state power; instead, it is horizontally recognized by those who both create law and are subject to law. As stated by Brunnée and Toope, "the interactional theory of law explains that it is obligation that constitutes law's added value, not form, and that a sense of obligation will only arise when states and other actors perceive lawmaking to be legitimate."[757] This theory reveals that law is not a product that is manufactured in centralized, hierarchical systems and merely distributed to social actors for consumption. Citizens in domestic systems and States, along with other actors at the international level, are not consumers. They are active agents in the continuing enterprise of lawmaking through the elaboration of custom and soft law.

3.6 Take-Away on the Applicability of Self-Regulated Norms (Soft Law) in ISDS Tribunals

In keeping with reality in the globalized world including the erosion of the fundamental pillars of the traditional legal order, sociolegal scholars promote debates about the importance of transnational norms developed out of constant interactions among States and non-state actors without going through the authoritative act of state consent. Building upon this scholarly debate, I propose transnational self-regulated norms as transnationalized customary international law that not only cannot be ignored but must be considered by ISDS tribunals as *applicable* law in resolving investment disputes and interpreting IIAs. My proposal touches on the institutional and normative capacity of the legal system to play a potentially decisive role in upholding foreign investors environmentally responsible at the transnational level. These objectives make our

[755] *Ibid*.
[756] *Ibid* at 55.
[757] *Ibid*.

endeavors not only an effort at theorizing transnational law regimes but also highly practical in applying transnational self-regulated norms in ISDS tribunals.

To examine the lawmaking power of non-state actors and the legitimacy of (hybrid) non-state-based norms, legal pluralism has been the entry point to challenge the state-centric notion of law at the transnational level. The hybrid theory further opens a promising avenue to explain the participatory role of non-state actors even where States are still central and to describe the institutional dimension of transnational law. In addition, the interactional theory contributes to explaining the legitimacy of transnational norms that are developed through interactional communities. This discussion has introduced a theoretical framework for examining how and under what conditions transnational self-regulated norms may become legal rules to govern new transnational relationships that do not fit easily into the existing dominant analytical scheme of state-state or private-private relations as well as providing a reference point for demanding that ISDS tribunals pragmatically apply these transnationalized customary international norms (rules of law) to investment disputes.

Transnational self-regulated norms, therefore, would be institutionalized when State and non-state actors cooperate to develop (hybrid) non-state-based norms that aim to protect justice and promote efficiency in the economic sector. These norms would then be legitimized when they adhere to the criteria of legality and their subjects, who have created them, reciprocally fulfill duties while developing a sense of obligation towards the norms. Indeed, transnational self-regulated norms may possess more obligatory force than state-based law "when norms are rooted in shared understandings and adhere to the conditions of legality" to generate fidelity.[758] This theoretical analysis of transnational law can explain why lawmaking participants comply with a legal system, even when it pursues a particular policy with which individual participants disagree. It is due to the reason that they believe they have effectively engaged in the lawmaking process and that adherence to the criteria of legality limit the arbitrary exercise of power. Therefore, in this bottom-up lawmaking process at the transnational level, actors are not merely

[758] *Ibid* at 51.

consumers of law; instead, they are active agents in the ongoing enterprise of lawmaking, through building shared understandings and continuing practice of legality.[759]

Accordingly, transnational self-regulated norms can be rendered as rules of law and, in other words, become transnationalized customary international law, although they have not been expressly acknowledged by state or interstate consent as formal law. These norms then govern global relations based on shared understandings arising from consistent interactions among diverse participants and anchored in stable patterns of expectation between involved entities. As a corollary, transnational self-regulated norms will be of limited capacity to govern global interactions mostly if restricted participants were involved in the norm-building process and insufficient attention were paid to the requirements of legality—which causes transnational self-regulated norms to deviate markedly from the common practices and shared understandings of society, to be unintelligible to their addressees , and to destroy a sense of obligation (fidelity) towards the norms.

Building on the theoretical framework developed in this chapter, which draws from legal pluralism, the hybrid theory, and the interactional theory to posit the transformative potential of transnational self-regulated norms (i.e. to be understood as law), I will now delve into a juridical analysis of a prominent transnational self-regulated norm that is highly relevant to the field of investment law, the UNGC. In Chapter 4, I intend to demonstrate how, despite engaging non-state actors and the lack of formal state consent to underpin the UNGC, the UNGC can be considered as transnationalized customary international law by ISDS tribunals and then be applied in resolving the substantive aspects of investment disputes. Consequently, this provides tribunals with a principled foundation to incorporate environmentally responsible standards into the resolution of investment disputes and the interpretation of IIAs.

[759] Adler, *supra* note 738; Roger Cotterrell, "Transnational Communities and the Concept of Law" (2008) 21:1 Ratio Juris 1.

Chapter 4: Engaging Self-Regulated Norms in Investment Treaty Interpretation: Case Study of the United Nations Global Compact

4.1 Introduction

In recent decades, the growing empowerment of foreign investors—facilitated by the asymmetrical structure of investor-state dispute settlement (ISDS) tribunals—has constrained host States' ability to pursue their sustainable development goals (SDGs). This imbalance has prompted legal scholars to address the impeding role of ISDS tribunals for sustainable development and seek solutions that reconcile the competing priorities of investment protection and environmental considerations in the decision-making process of investment dispute cases. According to data published by the UN Conference on Trade and Development (UNCTAD), about 15 percent of all 1,190 known investment cases, at least 175 treaty-based ISDS cases, are tied to environmental measures.[760] In the majority of these investment disputes, foreign investors brought claims before ISDS tribunals alleging that host States implemented environmental measures that violated their investment-protection rights under IIAs and adversely affected investment activities. In their defence, host States often point out their environmental obligations behind the measures to justify their regulatory actions aimed at controlling environmentally risky activities. They emphasize that public interest demands our immediate attention and concerted efforts to protect the environment against the environmental misconduct of foreign investors. However, "in a globalized economy, the host state's ability to … regulate foreign investment effectively is often limited in practice."[761] As expansively discussed in Chapter 1, the widespread application of the *sole effects doctrine*, the restricted utilization of the *regulatory power doctrine*, and the infrequent recourse to the *investment reprisal approach*[762] by investment arbitrators in

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[760] United Nations Conference on Trade and Development (UNCTAD), *Treaty-based Investor–State Dispute Settlement Cases and Climate Action* (2022).
[761] Patrick Abel, *International Investor Obligations: Towards Individual International Responsibility for the Public Interest in International Investment Law* (Nomos Verlagsgesellschaft mbH & Co. KG, 2022) at 26.
[762] See Jarrett, *supra* note 191.

investor-state disputes thwart and/or weaken many host States' meaningful actions towards environmental protection.

Motivated by these concerns, I engage in the ongoing scholarly debate that critically examines the limitations of the current investment law regime. As scholars have pointed out, "[t]he regime of international investment law, as it currently stands, provides little opportunity to hold foreign investors accountable for those human rights, environmental, and labor violations that are pertinent to investment, as these subjects are rarely a part of investment treaties or investment contracts."[763] As emphasized earlier in this dissertation, I believe that the lack of enforceable obligations placed on foreign investors by IIAs is a fundamental flaw in the ISDS framework. This deficiency allows investors to operate with extensive legal protections, while host States face significant constraints on implementing public interest regulations, particularly those related to environmental protection and sustainable development. To address this imbalance, I propose that concerns regarding the environmentally risky behavior of foreign investors can be raised by host States in ISDS tribunals as breaches of those investors' own international obligations with a view to justifying the environmental measures that they have taken but that have been challenged by investors.

In my proposal, host States invoke self-regulated norms of transnationalized customary international law elaborated by transnational corporations and argue for foreign investors' non-compliance with their obligations under international environmental norms.[764] Allegations of illegal conduct on the part of foreign investors "might help a state defend itself from the investor's claims of fair and equitable treatment violations by demonstrating that the state's conduct was warranted because of the investor's actions."[765] Given the much-criticized lack of balance in investment arbitration and the difficulties faced by developing host States in regulating foreign investors' misconduct, host States may seek "to avoid their responsibility by challenging

[763] Yulia Levashova, "The Accountability and Corporate Social Responsibility of Multinational Corporations for Transgressions in Host States Through International Investment Law" 14:2 Utrecht Law Review 2018 at 40.
[764] Jean-Michel Marcoux, "Informal Instruments to Impose Human Rights Obligations on Foreign Investors: An Emerging Practice of Legality?" (2021) 34:1 Leiden Journal of International Law 109–126.
[765] Andrea K Bjorklund, "The Role of Counterclaims in Rebalancing Investment Law" (2013) 17 Lewis & Clark Law Review 461 at 465.

the claimant investor's socially responsible conduct" in ISDS tribunals.[766] In such cases, ISDS arbitrators are—within the framework I have been developing and will further develop in this Chapter—authorized to mutually consider foreign investors' investment protection rights and their environmental obligations to comply with international environmental norms. This challenge could move us towards holding investors environmentally accountable whereby, as Baltag discusses, a "[r]espondent State [may] invoke[] an investor's alleged non-compliance with environmental law/human rights law, making claims for compensation inadmissible."[767] The approach I propose is a practical, immediate, and comprehensive solution for holding foreign investors accountable for environmental impacts within ISDS tribunals and for making compensation inadmissible for foreign investors notwithstanding that the host States have taken actions against the financial benefits of foreign investors.

To achieve this objective, I build on and advance the discussion put forth by Jarrett, who articulates the rules on *post-establishment illegality defence*,[768] and Amianto, who uses the *clean hands doctrine* as legal foundation for the post-establishment illegality defence and claims that investors' serious violation of transnational public policy could result in a successful post-establishment illegality defence.[769] I argue that, by giving weight in dispute settlement procedures to self-regulated norms that directly impose international environmental obligations on foreign investors, a counterbalance will be created to mitigate the privileged position of foreign investors as mere rightsholders as a result of which foreign investors can be held environmentally responsible before investment tribunals. In other words, I will examine whether self-regulated norms developed mostly by transnational corporations—including through interaction to varying extents with States and interstate organizations can be considered transnationalized customary international law that imposes environmental obligations on foreign investors that must be given effect in the decision-making process of ISDS tribunals. Upon this examination, ISDS tribunals

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[766] Laurence Dubin, "Corporate Social Responsibility Clauses in Investment Treaties" (2018), online: *Investment Treaty News*.
[767] Crina Baltag, "Human Rights and Environmental Disputes in International Arbitration" (2018), online: *Kluwer Arbitration Blog* <https://arbitrationblog.kluwerarbitration.com/2018/07/24/human-rights-and-environmental-disputes-in-international-arbitration/>.
[768] Jarrett, *supra* note 191 at 110.
[769] Lodovico Amianto, "The Role of "Unclean Hands" Defences in International Investment Law" (2019) 6 McGill Journal of Dispute Resolution.

could involve self-regulated norms in the investment treaty interpretation process and consider such norms as "relevant rules of international law applicable in the relations between the parties" so as to resolve substantive aspects of investment disputes by taking into account *both* foreign investors' rights *and* their environmental obligations. Involving self-regulated norms in the investment treaty interpretation process in this way orients international investment law towards meeting SDGs by construing host States' environmental measures as a lawful response to foreign investors' lack of compliance with their international environmental obligations during the performance of investment activities.

Hence, in this Chapter, I examine how ISDS tribunals can hold foreign investors accountable for their post-establishment illegality of not complying with transnational environmental initiatives. Particularly, I explore how transnational environmental initiatives—acquiring the legal status of transnationalized customary international law and binding investors under international law—can be invoked to require compliance or restraint from environmentally harmful actions. Building on the doctrinal and theoretical analyses in Chapter 2 and Chapter 3, I take a practical approach by introducing the United Nations Global Compact (UNGC) as a cluster of *relevant* rules of transnationalized customary international law *applicable* in the relationship between foreign investors and host States to resolve the substantive aspects of investment disputes. The UNGC thereby represents liability law capable of resolving some of the substantive aspects of investment disputes between foreign investors by virtue of imposing direct international environmental obligations on foreign investors.

The discussion begins by explaining the post-establishment illegality defence, a legal doctrine that is already available to be used by host States in ISDS tribunals in order to demonstrate that foreign investors have violated their international environmental obligations. I then thoroughly analyze two major legal constraints facing ISDS tribunals' examination of the relevance and applicability of self-regulated norms in the dispute resolution process: Relevance means whether liability law is sufficiently related to the issues of investment law (investment dispute and/or investment treaty)—in the combined sense discussed in Chapter 2, of "sameness" of subject-matter according to contextual, purposive, and value-sensitive characterizations of a field and absence of actual conflict between a given norm in the treaty and the otherwise relevant

customary norm—and applicability means whether liability law is both opposable as between and legally binding on the disputing parties. Next, the Chapter introduces the UNGC as an existing self-regulatory framework that imposes international environmental obligations directly on foreign investors. I further evaluate the potential of the UNGC to be considered as more than simply a transnational normativity shy of being law—that is, as transnationalized customary international law—and thus to be treated as relevant and applicable by ISDS tribunals in the treaty interpretation process.

Ultimately, this analysis has laid the groundwork for future investment arbitration to take a more balanced approach by ensuring that foreign investors are held accountable for environmental harm**,** rather than solely benefiting from investment protections. The three key contributions are:

1. Recognition of Foreign Investors' Environmental Obligations: By incorporating self-regulated norms into investment arbitration, this research challenges the traditional asymmetry in international investment law. It establishes that foreign investors not only hold rights under investment treaties but also bear direct environmental responsibilities under general international law. This shift ensures that ISDS tribunals take into sufficient account investors' obligations to avoid environmental destruction in order to prevent them from benefiting from investment protections despite engaging in harmful activities.
2. A Legal Basis for Eliminating Investor Compensation: This analysis provides a framework for host States to invoke the post-establishment illegality defence, allowing ISDS tribunals to eliminate monetary compensation awarded to investors who have engaged in environmentally harmful conduct. By integrating general international environmental law into treaty interpretation, this approach ensures that foreign investors cannot misuse ISDS mechanisms to undermine legitimate environmental regulations imposed by host States.
3. Opening the Door for Host States to File Counterclaims: Perhaps most significantly, this research establishes a pathway for host States to bring counterclaims against foreign investors in ISDS tribunals.[770] By demonstrating that foreign investors can be held

[770] Counter-claiming is a clearly available in virtually any investment treaties. The situation of investment treaties that have been drafted so as to allow States to initiate claims themselves—i.e. not to have to wait for a claim before invoking its own claim of wrongdoing—is not as pervasive. However, where a treaty has been drafted to give ISDS tribunals jurisdiction over any investment dispute—and is not carefully limited only to breach of the treaty itself—

accountable for environmental harm, host States not only can defend against investor claims but also can seek compensation for environmental damage caused by foreign investments. This finding strengthens the obligations of foreign investors in arbitration, promoting a fairer and more sustainable dispute resolution system.

Together, these findings provide what I believe to be a novel legal framework that shifts investment arbitration towards a more equitable and environmentally responsible model—one that reclaims foreign direct investment (FDI) one of the principal means of financing the *2030 Agenda for Sustainable Development* and its 17 Sustainable Development Goals.

4.2 Post-Establishment Illegality Defence

The current landscape of the international legal system has witnessed a profound transformation characterized by the decentralization of power and a departure from traditional hierarchical structures, as authority and influence diffuse across diverse actors, platforms, and contexts. This transformation was and continues to be primarily driven by processes of economic globalization, which are challenging the traditional centrality of the State as the main subject of and authority in the international legal system. In this reconfiguration, corporate entities have gained immense power, often on par with or even surpassing many States. In this context, the OECD's recent report, *Revenue Statistics 2020*, provides empirical data on corporate revenues compared to national GDPs and shows that the top 100 multinational corporations generated nearly $10 trillion in revenues, accounting for almost 20% of global GDP.[771] For example, in the fiscal year

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then the door is opened not only for invoking investor obligations through the post-establishment illegality defence or by counterclaim but also by a proactive claim of breach of international law. An example of a treaty drafted with this wider form of jurisdiction is that in play in the *Urbaser* case, the treaty between Argentina and Spain. Article X(1) of the agreement, note 113, provides:

> Disputes arising between a Party and an investor of the other Party in connection with investments within the meaning of this Agreement shall, as far as possible, be settled amicably between the parties to the dispute.

In the Urbaser case, the tribunal then asserted: "This provision is completely neutral as to the identity of the claimant or respondent in an investment dispute arising 'between the parties.' It does not indicate that a State Party could not sue an investor in relation to a dispute concerning an investment," *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*, *supra* note 3 para 1143.

[771] Organization for Economic Co-Operation and Development (OECD), *Revenue Statistics 2020* (2020), online: <https://doi.org/10.1787/8625f8e5-en.>.

ending January 31, 2023, Walmart reported revenues of $611.3 billion.[772] It shows that Walmart's annual revenue exceeds the total economic output of countries like Belgium and Thailand, underscoring the significant economic influence multinational corporations can wield on a global scale.[773]

Beyond their economic power, multinational corporations exert substantial influence over legislative processes and enjoy extensive international rights and protections. A 2023 study from King's College London critically examines how these entities shape international legal frameworks, often perpetuating hegemonic patterns that prioritize corporate interests, and enjoy a wide range of international rights and institutional protection including protection emanating from their home State(s).[774] Furthermore, many lawmaking processes at the transnational level, such as the development of UNGC, that characterizes a form of global governance, are directly associated with the increased involvement of multinational and transnational corporations.

The combination of enormous economic resources and political lobbying allows multinational corporations to operate with a degree of autonomy and influence that can rival or even exceed that of sovereign states. In addition, with a scientific understanding of investments' impacts on environmental degradation and an increasing acknowledgment of the responsibilities of investors as corporate citizens to the communities in which they operate, States should no longer be viewed as the sole entities responsible for environmental protection.[775] This dynamic raises important questions about accountability, governance, and the balance of power in the global arena. As an outgrowth of a deepening ethical view, corporations, alongside States, are increasingly considered to be environmentally responsible as a matter of law at the international level.

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[772] *2023 Financial Fact Book*, by Corporate Home Office (Walmart Inc, 2023) online: <https://s201.q4cdn.com/262069030/files/doc_downloads/Factbook/2023/FY23-Financial-Fact-Book.pdf?utm_source=chatgpt.com>.
[773] International Monetary Fund (IMF), "World Economic Outlook Database" (2023), online: <https://www.imf.org/en/Publications/WEO/weo-database/2023/October>.
[774] Rute Passos, "The Influence of Multinational Corporations on the International System" (2023), online: *King's College London* <https://www.kcl.ac.uk/the-influence-of-multinational-corporations-on-the-international-system?utm_source=chatgpt.com>.
[775] See Shawkat Alam & Abdullah Al Faruque, *Foreign Investment, Human Rights and Environmental Protection: Striking a Balance for Sustainable Development* (New York: Routledge, 2025).

This is the crucial entry point to address asymmetries in investment law—providing international rights to investors without imposing international obligations—and recognize the duty of investors to protect the environment in international investment law jurisprudence. As an extension of this development (moving from the ethical to the legal realm), environmental illegalities committed by an investor after establishing the investment, can provide the basis both for holding the foreign investor environmentally responsible and for exonerating the host States from compensating foreign investors in ISDS tribunals. Through the defence of post-establishment illegality, foreign investors may be rendered liable for violating the environmental rights of host States.[776]

4.2.1 Definition and Doctrine

The concept of post-establishment illegality defence is advanced by Jarrett, in his monograph, *Contributory Fault and Investor Misconduct in Investment Arbitration*, who explains that "a plea of post-establishment illegality is founded on investor (mis)conduct in breach of a liability rule."[777] Jarrett's work is the bedrock of my argument that an investor's own illegal or wrongful conduct can serve as a defence for the host State's actions. His work effectively guides me towards using the investor's illegality as a sword—a proactive and independent basis for a defence. This is a significant step away from traditional ISDS interpretations that focus almost exclusively on the host State's obligations to the investor, often overlooking the investor's own legal and ethical responsibilities. I am taking Jarrett's initial crack opened in the traditional ISDS

[776] Post-establishment stage matters here, because, at this stage of investment, rules of international law are often applied by investment arbitrators as substantive law. Despite the existence of the investment reprisal defence as another avenue for justifying host States' breach of investment treaties, in this study, I focus my attention on the avenue of the post-establishment illegality defence. Briefly speaking, in the investment reprisal defence, an investor's egregious conduct violates *domestic law*, affronts the host State's sovereignty, and then provokes the host State's breach of the investment agreement. Crucially also, investment reprisal involves sovereign responses to misconduct. It means the investor's misconduct has motivated the host State's conduct. Therefore, investment reprisal concerns conscious responses to misconduct that compromises the host State's sovereignty, whereas post-establishment illegality is more concerned with notions of legality: one is about sovereign power and causality, the other about legality and compliance with law. Although the investment reprisal defence might be a potential option relevant to the liability question and for re-evaluating the conduct of the host State, it is a weak rebuttal to hold foreign investors environmentally responsible before ISDS tribunals for two reasons: first, as discussed in Chapter 2, the involvement of domestic law in ISDS tribunals as substantive law often fails due to the primacy of international law in the dispute settlement process; second, the major objection facing this line of defence is the possibility of the host State engaging in another kind of reaction than violating investment agreement as the chosen form of retaliation against the foreign investor's wrongful conduct. See Chapter 5 in Jarrett, *supra* note 191.

[777] Jarrett, *supra* note 191 at 111.

framework and widening it to create a new and more robust pathway for integrating environmental considerations into the ISDS decision-making process. Thus, I use the post-establishment illegality defence to argue that, instead of the host State saying, "Our environmental measure was justified because the investor was acting illegally," the host State can say, "The investor's claim is invalid" or "I will not fully compensate the investor because its ongoing operation is characterized by illegal conduct." It is a legal argument used by host States in ISDS tribunals to challenge an investor's claim by asserting that the investor has engaged in illegal or non-compliant conduct after the establishment of the investment.

To establish the potential grounds for holding foreign investors accountable for international environmental violations in investment tribunals, it is crucial to develop the doctrinal foundation of the plea of post-establishment illegality as a defence mechanism that raises the illegal conduct of investors during the performance of their investment activities. While Jarrett's argument is pioneering and fundamentally important for establishing the principle of investor responsibility, it struggles to find a firm foothold in existing international legal principles. To strengthen and operationalize the notion of post-establishment illegality defence, I will engage with the clean hands doctrine as used by Amianto in the context of investment tribunals.[778] Amianto's work provides an important doctrinal layer by arguing that a claimant's right to seek relief is fundamentally contingent on their own lawful conduct.

Post-establishment illegality defence—whether for breach of obligations by States or by other actors that owe obligations to States—is not discussed in the ILC Articles on State Responsibility, however, some academic literature extends the defence of illegality, the general principle that a person should not be permitted to profit from his or her own illegality, to post-establishment illegality and grounds its existence in the same principle.[779] Most importantly, in the context of investment law, some scholars, who believe that the illegality principle, which mostly concerns unlawful conduct of investors at the establishment stage of investments, is in fact a disguised expression of the clean hands doctrine. They argue that the clean hands doctrine holds significant importance as a useful corrective, capable of making a meaningful contribution

[778] Lodovico Amianto, "The Role of "Unclean Hands" Defences in International Investment Law" (2019) 6 McGill Journal of Dispute Resolution.
[779] Jarrett, *supra* note 191 at 109.

to holding foreign investors internationally responsible during the post-establishment phase of their investment.[780] The clean hands doctrine that forms part of the legal consciousness of both civil and common law jurisdictions—and that thus, within international law, has the pedigree of a general principle of law—was developed as a means to avoid an opportunistic claimant profiting despite its illegal conduct.[781] If a party has unclean hands by being engaged in a certain type of illegality related to its own claim, the clean hands doctrine will prevent that party from benefiting from its own illegal behavior.[782] Otherwise, "allowing a plaintiff with unclean hands to recover in an action creates doubts as to the justice provided by the judicial system."[783] Given the lack of consensus on whether the illegality principle originates from the unclean hands doctrine or relates to separate concepts, in this Chapter, I aim to introduce the clean hands doctrine as one foundational doctrine for the plea of post-establishment illegality as an aspect of applicable substantive law for holding foreign investor internationally accountable in ISDS tribunals—versus the standard understanding of clean hands as only serving as an equity-based reason to deem a claim inadmissible or a tribunal without jurisdiction (as will be elaborated below).[784]

Allegations of investment illegality are of paramount importance in investment disputes and present investment tribunals with significant challenges with regard to jurisdictional competency, claims admissibility, and the merits of disputes—and the blurred lines dividing those three dimensions or phases of disputes. Below, by briefly referring to key investment dispute cases and prominent academic arguments, I present two scenarios where host States employ the defence of investment illegality, at both establishment and post-establishment stages of investment. In these scenarios, the tribunals have relied on the clean hands doctrine to either reject their competency

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[780] Patrick Dumberry & Gabrielle Dumas-Aubin, "When and How Allegations of Human Rights Violations Can be Raised in Investor-State Arbitration" (2012) 13:3 The Journal of World Investment & Trade 349–372.
[781] T Leigh Anenson, "Announcing the "Clean Hands" Doctrine" (2017) 51 University College Dublin Law Review 1827.
[782] Agata Zwolankiewicz, "The Principle of Clean Hands in International Investment Arbitration: What is the Extent of Investment Protection in Investor-State Disputes?" (2021) 3 Investment Treaty Arbitration in Review 4 at 5.
[783] *Kendall-Jackson Winery Ltd v Superior Court,* 90 Cal Rptr (2d) (CA Cal 3 December 1999), at 749.
[784] To find discussions on the main unresolved issues surrounding the relevance of the clean hands doctrine in international law and its connection to the illegality principle, see Marcin Kaldunski, "Principle of Clean Hands and Protection of Human Rights in International Investment Arbitration" (2015) 4:2 Polish Revie and International and European Law 69; Amianto, *supra* note 769; Zwolankiewicz, *supra* note 782.

to hear the case, render particulate claims inadmissible, or (as a merits issue) reduce compensation owed by the State to the investor.

In the first scenario, during investor-state arbitration proceedings, the host State raises the defence of investment illegality as a bar to challenge the jurisdictional competence of the investment tribunal for resolving the dispute. In its defence, the host State argues that foreign investors have unclean hands because their investments, at the establishment stage, violate the national laws and regulations of the host State, which would then prevent them from receiving treaty protection in ISDS tribunal.[785] To decide on a dispute, if the illegality occurs at the establishment phase of the investment and if the investment was not established in accordance with the national law of the host State, the investment is assumed to be directly based on its own illegal act from the outset. In such cases, investment arbitrators most likely dismiss the dispute on a jurisdictional basis. That is because illegal behaviour at the establishment stage can result in the investment project not being qualified as an investment within the meaning of the treaty. As a result, the arbitral tribunal may decline its jurisdictional competence *ratione materiae* (there being no object on which to found the dispute).[786] In this establishment-stage scenario, investment tribunals often refer to the Latin maxims such as "*ex dolo malo non oritur actio*" (an action does not arise from fraud or, more broadly and more accurately, an action does not arise from a base cause) and "*nemini dolos suusprodesse debet*" (nobody may profit from his own fraud or, more broadly again, nobody may profit from their own wrongdoing). Where one extends the clean hands doctrine to matters beyond literal fraud, the broader maxim *ex turpi causa non oritur actio* (no cause of action can arise from a wrongful act) best expresses the logic. The clean hands doctrine, however framed in Latin, leads to the conclusion that the investor's illegal conduct forfeited the right to invoke protection under investment treaties.[787] Here, the

[785] See Chapter 2 for the discussion about the role of national law in investment disputes to define the concept of investment.
[786] There have been numerous instances where an investment tribunal has been called to apply, mostly as a jurisdictional objection, a legality requirement provision: see Amianto, *supra* note 772 at 8. In *Inceysa*, the tribunal was faced with that question and determined that the "in accordance with the law" provision embodied in the Spain-El Salvador BIT was a "necessary condition for an investment to benefit," Inceysa Vallisoletana SL v El Salvador, ICSID Case No ARB/03/26, Award 2 August 2006. Since the dispute stemmed from an illegal investment, it fell outside of the consent to arbitrate granted by the parties, *ibid* para 207.
[787] *Inceysa Vallisoletana SL v. El Salvador,* ICSID Case No ARB/03/26, Award 2 August 2006, *supra* note 786 para 240; Nelson Enonchong, "Effects of Illegality: A Comparative Study in French and English Law" (1995) 44:1 International & Comparative Law Quarterly 196–213.

clean hands doctrine is an expression of the illegality principle. It means that the illegality principle—here, at the establishment stage—is a disguised expression of the clean hands doctrine—or, put differently, not so much disguised as given another label—by means of which the tribunal dismisses its jurisdictional competence for the dispute settlement.[788]

In the second scenario, when the foreign investor brings the claim before the ISDS tribunal for the host State's alleged violation of investment protection, the host State accuses the foreign investor of illegal conduct happening at the post-establishment stage of investment activities due to the investor's lack of compliance with international law.[789] In its defence, the host State invokes the international obligations of the foreign investor and argues that the investor violated such obligations during the performance of investment activities.[790] The host State then seeks to either make the claim inadmissible because of the investor's international illegal conduct (and thus, in the result, to avoid any compensation being owed because the case is dismissed) or exonerate itself from paying compensation to the foreign investor. On the latter argument, the State ultimately seeks illegality to operate as a full defence—and thus exoneration from paying any compensation. However, the question arises of whether, if the matter is dealt with at the merits stage as and not as a jurisdictional or admissibility dismissal, the defence can operate only as a partial one in that compensation owed by the State for its own wrongdoing may be more than what the investor owes the State for the investor's wrongdoing. The defence can be considered partial also in the sense of a contingent relationship with the question of whether the State can wholly avoid paying any compensation at all—something that is possible but depends on the comparative assessment of the respective compensations each owes the other. This *whole versus partial* defence question will be discussed briefly below.

To decide on the post-establishment illegality conduct of the investor due to violations of international obligations, the investment tribunal would refer to the clean hands doctrine in a form well-depicted by the maxims *nemo auditur propriam turpitudinem allegans* (no one can be

[788] Dumberry & Dumas-Aubin, *supra* note 780.
[789] It should be emphasized that the obligations being breached by foreign investors must be international-law ones; otherwise, the doctrinal issues would be that of investment reprisals in response to breaches of domestic law. See Chapter 1 on this matter.
[790] Jarrett, *supra* note 191.

heard to invoke his own turpitude) or the already-referenced *ex turpi causa non oritur actio* (where the idea of a cause of action not arising is treated more generally as the idea that illegality undermines the substantive merits of the claim in one way or another).[791] Here, the investment tribunal acknowledges its jurisdictional competency to decide the investment case, because non-compliance with international norms does not deprive the investment of its status under the investment treaty. But the plea of post-establishment illegality impacts either the admissibility of the claim[792] (similar, albeit not identical, to finding no subject-matter jurisdiction) or plays a role with regard to the merits of the dispute.[793] Either of such decisions, as noted by Bjorklund and Vanhonnaeker, shows that ISDS tribunals use international law while referring to the clean hands doctrine.[794] More specifically, Dumberry and Dumas-Aubin clearly state their opinion that violations of international human rights should impact the protection under the treaty during the post-establishment phase of the investment and result in the inadmissibility of an investor's claim "precisely because of its unacceptable behaviour."[795] Zwolankiewicz also argues "with regard to the issue of the clean hands principle, especially in the context of violation of human rights, that the actions of the parties should also impact the protection under the treaty during the post-establishment phase of the investment."[796]

Inadmissibility of the claim concerns "the power of the tribunal to decide a case at a particular point in time in view of possible temporary or permanent defects of the claim."[797] With regard to the admissibility of the claims—when investors' misconduct happened during the post-establishment phase of the investment, as opposed to its establishment—the tribunal is concerned

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[791] Amianto, *supra* note 769.
[792] Maintaining that corruption violates international public policy, the tribunals in *World Duty Free Company Limited v. Kenya, I*CSID Case No ARB (AF)/00/7, Award 4 October 2006, *Spentex Netherlands BV v. Republic of Uzbekistan,* ICSID Case No ARB/13/26, Award 27 December 2016, and *Metal-Tech Ltd v Republic of Uzbekistan,* ICSID Case No ARB/10/3, Award 4 October 2013 dismissed all investors' claims due to their lack of compliance with international law after the establishment of investment activities. In the tribunal decisions of these cases, "transnational public policy has been explicitly recognized by investment tribunals, and that the violation of public policy has consistently resulted in the decision to dismiss all the investor requests:" Amianto, *supra* note 769 at 22.
[793] Filip Balcerzak, *Investor–State Arbitration and Human Rights* (Brill | Nijhoff, 2017) at 147.
[794] Andrea K Bjorklund & Lukas Vanhonnaeker, "Yukos: The Clean Hands Doctrine Revisited" (2015) 2 Diritti umani e diritto internazionale 365–386.
[795] Dumberry & Dumas-Aubin, *supra* note 780 at 362.
[796] Zwolankiewicz, *supra* note 782 at 9.
[797] Aloysius Llamzon & Anthony Sinclair, "Investor Wrongdoing in Investment Arbitration: Standards Governing Issues of Corruption, Fraud, Misrepresentation and Other Investor Misconduct" in A J van den Berg, ed, *Legitimacy: Myth, Realities, Challenges* (Kluwer Law International, 2015).

with particular claims being allowed to proceed where the tribunal accepts general jurisdiction whereas with jurisdictional objections, the tribunal's general competence to hear the dispute at all is involved.[798] That said, even if the tribunal has the jurisdiction to hear a dispute, it will not adjudicate the merits of the case; in that way inadmissibility resembles the lack of jurisdiction of the arbitral tribunal as in both instances the claim will be dismissed prior to the analysis of the merits.[799]

However, if the tribunal does not decline its jurisdiction to hear the dispute and also finds the claim admissible, the unclean hands of the investor may yet have an influence over the merits of the case.[800] Certain actions of the investors may not have a direct impact on jurisdiction or admissibility of the claim but "have negative consequences with regard to the merits of the case, such as resulting in a reduced compensation."[801] As suggested by the phrase "reduced compensation," the illegal conduct having escaped invocation by the tribunal as a basis—either on jurisdictional or admissibility grounds—of complete dismissal of the claim, the question arises as to whether the tribunal can consistently treat the same illegality as a basis for a full defence on the merits (exoneration and no compensation at all owed) or whether the tribunal may or even must approach the matter as one of proportionate reduction in the amount of compensation owed by the State by looking at factors such as the causal relationship between the investor's illegal conduct and the State's measures against the investor, the relative seriousness of the illegality versus the harm to the investor, and so on. The better view would seem to be that it produces

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[798] In *Copper Mesa*, when determining the applicability of the clean hands doctrine, "the tribunal … referred to other facts which occurred in the post-establishment phase:" Amianto, *supra* note 769 at 11. Aloysius Llamzon & Anthony Sinclair, "Investor Wrongdoing in Investment Arbitration: Standards Governing Issues of Corruption, Fraud, Misrepresentation and Other Investor Misconduct" in A J van den Berg, ed, *Legitimacy: Myth, Realities, Challenges* (Kluwer Law International, 2015) at 530.

[799] Fabio G Santacroce, "Navigating the Troubled Waters Between Jurisdiction and Admissibility: An Analysis of Which Law Should Govern Characterization of Preliminary Issues in International Arbitration" (2017) 33:4 Arbitration International 539–570.

[800] *Fraport AG Frankfurt Airport Services Worldwide v The Republic of the Philippines,* ICSID Case No ARB/03/25, Award, 16 August 2016; Aloysius Llamzon & Anthony Sinclair, "Investor Wrongdoing in Investment Arbitration: Standards Governing Issues of Corruption, Fraud, Misrepresentation and Other Investor Misconduct" in A J van den Berg, ed, *Legitimacy: Myth, Realities, Challenges* (Kluwer Law International, 2015).

[801] Zwolankiewicz, *supra* note 782 at 4. In *Copper Mesa v Ecuador,* while agreeing with the Respondent's position that the claimant's post-acquisition conduct fell under the scope of the clean hands doctrine, the tribunal considered that it was more appropriate to connect this argument to the merits phase: *Copper Mesa Mining Corporation v. Republic of Ecuador,* Permanent Court of Arbitration (PCA) No. 2012-2, Award 15 March 2016, *supra* note 235 para 5.62.

reduction not exoneration, but with the important caveat that the nature of the illegality, its causal connection to the measures by the State, and its proportionate seriousness could well lead to the conclusion that reduction should be total—that no compensation should be owed. Such full reduction would not be automatic exoneration but the result, in terms of amount the State owes, would be *de facto* the same. A further virtue of the reduction-not-automatically-full defence approach is that this allows the question of compensation to slide into a counter-claim: if the State files a counter-claim for the illegal conduct and the compensation it owes is reduced to zero on the claim, then the possibility is open for the State to go on to recover money and not simply be content with not paying out anything.

Leaving aside the doctrinal debate of the above-mentioned scenarios and any further discussion, it is important to note that international law imposing obligations on foreign investors has been explicitly recognized by investment tribunals as substantive law, the breach of which is important for deciding whether the foreign investor has unclean hands. In this context, Amianto introduces the concept of transnational public policy as the most likely potential ground for making the claims inadmissible in ISDS tribunals. He argues that the concept of transnational public policy has been developed in the framework of international commercial arbitration and thus should be applicable in the context of treaty-based claims. In his view "ICSID tribunals have not only the possibility, but the obligation to prevent the enforcement of any arrangement which is contrary to a principle of transnational public policy because 'ignoring or tolerating illegality in such situations can be seen as contributing to distortion and suppression of competitive forces as well as discouragement of future investment'."[802] Amianto thus states that the ISDS tribunals would maintain that the violations of transnational public policy lead to dismissal of the claim.

While acknowledging Amianto's crucial role in introducing the concept of transnational public policy as a potential ground for making claims inadmissible in ISDS tribunals, I note a significant gap in his argument. Amianto correctly asserts that this concept, developed in the context of international commercial arbitration, should be applicable to treaty-based claims. However, his assertation suffers conceptual vagueness. He introduces the notion of transnational public policy but provides little to no substantive explanation of what it entails—including how it might draw

[802] Amianto, *supra* note 769 at 21.

on public international law norms—or how these principles should be engaged within an investment dispute. For example, as is debated within regular private international law's (conflict of laws) use of public policy or order public of the forum, can "public policy" be ahead of the crystallization of law and/or can it apply existing legal norms by analogy even if they do not apply directly (e.g., whether constitutional rights only owed by the State can be used as basis for public policy reasons not to endorse private conduct based on a foreign law). This lack of a clear, operational definition leaves the concept as a powerful but ultimately underdeveloped idea.

My contribution here is to fill this definitional and practical void. I argue that Amianto's notion of transnational public policy is, in essence, a reflection of transnationalized customary international law. By framing transnational public policy in these terms, we move beyond a vague, aspirational concept and ground it in concrete, legally recognized transnationalized customary international law. This prompts me to delve into the core question of whether transnationalized customary international law can hold foreign investors accountable for environmental violations in ISDS tribunals.

In the rest of this chapter, I will explain that the defence of post-establishment illegality can be successful if the norms violated by investors and then invoked by host States are rules of international law that impose direct international environmental obligations on investors. I will then explore whether the UNGC can be treated as transnationalized customary international law that constitutes a valid ground for the application of the post-establishment illegality defence—regardless of whether it results in no jurisdiction, in claim inadmissibility, or in compensation reduction (or even leads to the State receiving compensation under a counterclaim or, where the IIA permits, a claim that it proactively initiates).

4.2.2 Key Aspects and Significance

As its name suggests, the illegal conduct for post-establishment illegality requires the breach of a liability rule. Post-establishment illegality is a concept that seeks to promote the rule of law, particularly as it applies to the investor. For this reason, it is activated by a breach of an established liability rule applicable to the investor with the aim of holding the investor accountable for their legal obligations under international law. Within the context of this

dissertation, if a foreign investor violates liability law that involves international environmental law after the acquisition of the investment, the host State may implement regulatory measures to address the environmental violation. Here, the investor's illegal conduct has not motivated the host State's conduct for take regulatory measures. Instead, "it is an application of the relevant rule's dictates—a process governed by the rule of law, not any causal notions, because there is no causality between a breach of a rule and the subsequent legal consequence."[803] Therefore, although the regulatory measures would initially seem to amount to the breach of investment protection, the host State can defend itself by raising the post-establishment illegality conducts of the foreign investor. If the ISDS tribunal treats such international environmental law (liability law) as substantive law, foreign investors' claim of host States' alleged violation of investment treaty will be rendered inadmissible or compensation requested by foreign investors will be rejected or reduced.

If ISDS tribunals decide to dismiss the claim, the plea of post-establishment illegality analogously works as a full defence by way of depriving foreign investors investment protection under investment treaties. Since admissibility is fundamentally concerned with a claim's readiness for adjudication, not with deciding about the rights and wrongs of host States' conduct underlying the claim, the tribunals would not determine host States' liability, even if the host State's conduct appears to violate the treaty. However, in case of finding the claim admissible, tribunals have to decide about the liability of parties at the merit stage of the dispute. Although it is beyond the scope of this dissertation to detail how ISDS tribunals evaluate host States' regulatory measures taken in response to foreign investors' violation of international law, I briefly point out some integral issues with regard to this matter—leaving the particularities to the Jarrett book.

Jarrett acknowledges that the matter is not straightforward in practice, to this point in time. "[P]ost-establishment illegality entails the apportionment of liability–a task that arbitral tribunals have struggled with" and this mostly is due to the fact that arbitral tribunals enjoy much discretion when apportioning such that there is little by way of hard-edged rules or precedents that tribunals generate for each other.

[803] Jarrett, *supra* note 191.

In apportioning liability, the plea of post-establishment illegality ranges from full defence to full liability. As already noted, post-establishment illegality is rooted in legality, not causality, meaning that a host State's breach is not excused just because it follows investor misconduct. It must be done in accordance with applicable legal rules, including being proportionate and legally justified action. Another way to express this is that the illegality of the investor does not trigger a power of the State to adopt countermeasures that themselves may otherwise breach the law—it does not map onto the law of countermeasures between States.

For the defence to preclude or reduce liability, the State must demonstrate that its actions were based on established liability rules and not simply retaliatory. If a host State responds to an investor's illegality with disproportionate measures, the legal implications depend on whether the liability rule specifies a mandatory or discretionary consequence. If a discretionary legal consequence is involved, the host State's liability may still be reduced, but only if the response was proportionate to the investor's misconduct. However, if the host State's response is disproportionate, it cannot fully avoid liability unless the rule explicitly allows for such discretion. In contrast, if the rule prescribes a mandatory legal consequence for the investor's misconduct, the arbitral tribunal must recognize this and relieve the State of liability only to the extent the rule mandates—reducing the host State's liability accordingly, and potentially eliminating it altogether if the rule so mandates. In such cases of elimination, post-establishment illegality serves as a complete defence. Similarly, if the host State imposes a proportionate discretionary consequence, it may also be fully absolved of liability where the tribunal assesses that this is a proportionate outcome. This suggests the preclusion is more likely to be partial. The State may be relieved of liability only to the extent that its actions were necessary and proportionate responses under the rule of law, not excessive reactions to investor wrongdoing.

Raising the environmental obligations of foreign investors and holding them accountable before ISDS tribunals—through the post-establishment illegality defence—could serve as an important mechanism for recalibrating the balance between the rights and responsibilities of foreign investors. It moves beyond the notion of investors as mere right-holders, emphasizing their ongoing obligation to comply with environmental laws and standards throughout the duration of

their investment. This is even more the case if, alongside the defence, host States might invoke the post-establishment illegality defence to mount a counterclaim against investors, seeking compensation for environmental damages resulting from their investment activities and not simply seeking (via the defence approach) to eliminate any compensation allegedly due to the investor.) This defence would then bolsters the regulatory authority of host States, providing a legal mechanism to defend their environmental regulations and potentially avoid substantial financial penalties associated with successful investor claims. From the investors' point of view, the post-establishment illegality defence has the potential to act as a powerful incentive for investors to adopt socially and environmentally responsible practices to safeguard their treaty protections. It then encourages proactive compliance and sustainable behaviors with the investment sector.

4.2.3 Legal Constraints

However straightforward as the defence may seem, concerns emerge when a host State's claim of post-establishment illegality of conduct by the investor is based on a liability rule derived from international law, especially if that rule is rooted in customary international law. This is because, traditionally, such norms are understood to impose obligations only on States, not on private entities like investors. If this state-centric view holds, then international environmental norms cannot form a valid basis for a host State's defence of post-establishment illegality against an investor. Nevertheless, there has been a growing movement within international investment law to extend public international obligations to non-state actors, including investors. This trend raises a critical legal question: can investors be held directly accountable under international norms, thereby legitimizing their use in defence of post-establishment illegality?

It means that the effectiveness of post-establishment illegality defence ultimately hinges on whether the environmental obligations (liability law) exist as substantive law *relevant* to the investment disputes and *applicable* to foreign investors by ISDS tribunals. The success of this defence is then in the hands of investment arbitrators. They must determine whether rules of law imposing environmental obligations on foreign investors can be considered (a) law (thus, liability law) that is (b) relevant to investment disputes and (c) applicable between disputing parties. This involves a careful consideration of liability law in the investment treaty interpretation process,

potentially setting a precedent that could redefine the contours of environmental accountability in transnational investment litigation. In the following section, I will outline two significant legal constraints that ISDS tribunals must navigate when determining the existence and breach of liability law, and how these constraints may affect the viability of the post-establishment illegality defence.

The post-establishment illegality defence rests on two major legal rationales:

1. **Substantive environmental obligations exist at the international level:** The defence frames international environmental obligations of foreign investors as liability law within international law that goes to the substantive aspects of investment disputes. It contends that these obligations are integral to ensuring sustainable development and thus should be considered directly relevant and applicable in investment disputes—which is inextricable from the broader field of sustainable development law. Consequently, breach of these obligations by investors can justify the host States' violation of investment treaty and also trigger counterclaims by host States seeking redress for environmental harm.
2. **Foreign investors are subject to international law in the sense of having both rights and obligations:** It underscores that all parties, including foreign investors, are subject to the rule of law. If investors neglect their international environmental obligations, they cannot claim protection under IIAs as a shield against accountability. This is reinforced by the notion that non-state entities such as foreign investors s should be considered as subjects of international law by virtue of their involvement in the international law-making process. Consequently, international investment law must operate in harmony with substantive legal norms imposing environmental obligations on foreign investors.

According to the analysis laid out in Chapter 2 and Chapter 3, investment arbitrators are to determine liability law in light of Article 31(3)(c) of VCLT, which says international law, which obviously includes liability law imposing environmental obligations on foreign investors, should be taken into account for treaty interpretation if they are "relevant rules of international law *applicable* in the relations between the parties." For this reason, we considered in the earlier discussion that there are two legal constraints to be discussed when ISDS tribunals seek to re-

evaluate the conduct of host States in accordance with the liability law imposing environmental obligations on foreign investors:

- Is liability law *relevant*? (relevance means whether liability law is sufficiently related to the subject-matter of investment treaties)[804] and
- Is liability law *applicable*? (applicability means whether liability law is both opposable[805] as between and legally binding on the disputing parties)

4.2.3.1 Is liability Law Relevant to IIAs?

ISDS tribunals must begin by assessing host States' plea of post-establishment illegality defence with the question of whether international law (liability law) violated by foreign investors and then invoked by host States could be considered as a *relevant* rule of law in resolving the substantive aspect of investment disputes. Despite the practical importance of substantive law in resolving the investment disputes, ambiguities continue to exist over how ISDS tribunals manage interactions between rules of international law: international liability law and international investment treaty. Customary international law, beyond IIAs, is often applied in ISDS tribunals as substantive law to investment disputes.[806] To know how courts determining relevant rules of

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[804] Where I say "of investment treaties," I should also clarify that sameness of subject-matter should not be limited to a characterization of a specific investment treaty. The whole field of investment law matters to assess the sameness. However, since investment law is mostly comprised of investment treaties, if a rule of international law is relevant to the field of investment law, it is also relevant to investment treaties.

[805] Opposability, in the context of post-establishment illegality, refers to the ability to invoke and enforce liability law as between a given pair or set of actors—in our case, by States against foreign investors in investment arbitration. The basis for opposability is that international legal obligations are not merely aspirational or voluntary; they have legal force and can be invoked by other States or international entities to ensure compliance and seek remedies when violations occur. International legal obligations—once codified in treaties or recognized as part of customary international law—carry binding force. The principle of *pacta sunt servanda* (agreements must be kept) means that these obligations are not merely aspirational but are enforceable. Consequently, when a State enforces environmental or liability obligations, it is not acting on moral imperatives alone but on legal mandates that can be directly opposed to investors who have failed to comply. This concept is essential for maintaining order and accountability in the realm of international relations and ensuring that States adhere to their commitments under international law, Bjorge, *supra* note 549. Despite the importance of opposability in determining applicable law, due to overlaps between the notions of opposability and bindingness, in this chapter, I solely discuss legally binding status of liability law without further elaboration on opposability.

[806] Limiting the scope of my analysis to examine the applicability of only customary international law, rather than other sources of international law, notably treaty law, has roots in the primary objective of my study that seeks to evaluate the application of soft norms, which have evolved into transnationalized customary international law, in ISDS tribunals. That said, as the discussion of the post-establishment illegality defence makes clear, general principles of law is an international law source that is relevant to the existence and content of that defence (notably, how clean hands notions percolate up from most all legal systems to become part of the fabric of international law)—into which defence customary liability law is then inserted as the governing rules.

customary international law in the treaty interpretation process, my doctrinal analysis in Chapter 2 offers two consequential criteria:

1. sameness of the subject-matter of treaty law and customary international law, and
2. consistency as between rules of treaty law and customary international law.

In most ISDS cases, ICSID tribunals often interpret Article 42(1) of the ICSID Convention in a way that supports the primacy of international law as applicable law and among international rules, customary international law that a) deals with the *same subject-matter* as that of investment treaties and b) points to the *consistent* direction as investment treaties (without actual inconsistency) will be often considered as relevant rules of international law in resolving the substantive aspect of investment disputes.[807] Therefore, if liability law is categorized as a rule of international law but has a different subject-matter from IIAs or its requirements unavoidably conflict with the requirements of an investment treaty (which means there is an actual inconsistency between treaty law and other rules of international law), liability law would be classified as inapplicable (by virtually of being unrelated) for the purpose of the post-establishment illegality defence.[808]

4.2.3.2 Is Liability Law Applicable to Foreign Investors?

Notwithstanding the previous observation that in principle there is no difference between applying international law to States' conduct and to investor conduct, ISDS tribunals continue to grapple with whether liability law violated by foreign investors—and subsequently invoked by host States—can be considered an *applicable* rule of international law for resolving the substantive aspects of investment disputes. That is, they grapple with whether there are such international rules to apply, including at a general level of inquiry: is it even possible for investors to be saddled with obligations (outside the criminal law field) by international law?[809]

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[807] While there are far fewer examples of this being done with respect to the international legality of *investors'* conduct, there is no doctrinal or theoretical difference: if an international legal rule exists that creates investor obligations, then that rule is available for application no less than rules applicable to host States.

[808] Jarrett, *supra* note 191 at 129.

[809] The assumption that international law can directly impose obligations on foreign investors is challenged by what some call the validity issue. Validity issue arises if the liability law, which the host State alleges that the investor has breached, hails from international law, treaty law or customary international law. The invocation of treaty law as liability law would be rejected by ISDS tribunals in accordance with Article 34 of the Vienna Convention on the Law of Treaties: A treaty does not create either obligations or rights for a third State without its consent. Although an investor is not a third State as per this rule, there is jurisprudence indicating that third State includes non-state

This inquiry goes to the heart of the debate over the subjectivity of foreign investors to international legal norms.[810] It also raises critical questions about the nature of their obligations under international law because in the post-establishment illegality defence only those international rules which impose direct obligations can serve as applicable liability law in disputes.

Against the traditional understanding of international law, host States' plea of post-establishment illegality will be untenable unless host States can successfully allege that foreign investors have failed to comply with a rule of international law that imposes direct environmental obligations on those investors. As Chapter 3 was devoted to discussing, recent legal developments and returns to (generally ignored) longstanding accounts of the nature of international law suggest that transnational self-regulated norms emerging from interactions between States and investors can attain direct, binding force as legal norms. When these transnational norms—particularly those addressing environmental protection—are developed through consistent state-investor engagement, they are capable of acquiring the status of direct obligations that do not require state mediation for them to arise. My theoretical analysis in Chapter 3 provides a broader perspective on the institutional and normative structures of transnational self-regulated norms in order to be treated as applicable law in ISDS tribunals. Institutional structure of transnational self-regulated norms should be examined through the lenses of the "hybrid theory" that depicts transnational regulatory frameworks occupied by hybrid lawmaking powers, particularly in the face of growing transnational and non-state claims to normative authority. In addition, normative structure of

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entities, although this jurisprudence is sparse. Likewise, the invocation of customary law as liability law is faced with the validity issue because, like all liability rules, it imposes conduct obligations on their subjects, in the traditional international law only States can assume such obligations. Despite the assertion by some of a validity issue, in Chapter 3, the argument seems conceptually off-base. It seems to assume that non-state actors are in some kind of category of sovereign that obligations cannot be imposed on them by States—whether by treaty or by custom, or by complex, interactional, transnational processes involving States and non-state actors. This assumption is wrong and is belied by the many treaties that do place direct obligations on non-state actors, especially in the criminal law realm but also in realms like the law of the sea and international aviation law with respect to transportation craft and the corporations behind them. I thoroughly discuss how non-state actors could be both subject and object of international (transnational) law in order to consider international customary law as *applicable* liability law in the post-establishment illegality defence.

[810] Shao, *supra* note 246. This article discusses the lack of subjectivity of foreign investors to rules of international law and argues that the feasible solution for holding foreign investors accountable in ISDS tribunals is through the application of domestic law imposing obligations on foreign investors. However, my doctrinal analysis, in Chapter 2, thoroughly discusses the challenges facing the applicability of domestic law in ISDS tribunals for resolving the substantive aspect of investment disputes.

transnational self-regulated norms is examined in accordance with the interactional theory that proposes communal interaction among diverse actors and day-to-day perceptions of both social efficacy and foundational conceptions of substantive legality as integral elements to legitimize transnational norms.

The next section of this study will offer an in-depth case study examining the relevance and applicability of the UNGC as a potential source of transnationalized customary international law that may serve as liability law in investment disputes, entering into these disputes via the post-establishment illegality defence. I should make it clear that the case study of the UNGC does not exclude the study of other transnational self-regulated norms, which could be the subject of future research. The choice of the UNGC allows for a detailed exploration of one illustrative model, while leaving open the possibility of comparative or expanded analyses in subsequent work. Given the challenges that might be posed by the non-hybrid and non-interactional nature of other soft norms—such as the OECD Guidelines for Multinational Enterprises, which are developed primarily by the governments of OECD member countries with their environmental provisions drafted in a top-down manner—I consider the UNGC a particularly compelling example of a transnational self-regulated norm. The UNGC is distinguished by its hybrid institutional structure and interactional character, making it a strong exemplar of transnationalized customary international law. Below, I will further elaborate on the reasons for studying the UNGC as a potential source of liability law that could be invoked in support of the post-establishment illegality defence.

The UNGC, as a framework of voluntary guidelines and best practices, represents an evolving body of self-regulated norms (as one form of soft law)—developed through interactions among States and non-state actors—to address critical issues such as environmental protection, human rights, and corporate responsibility. While legal scholars highlight the important role of such soft law in reducing the inherent asymmetry between the protection of foreign investment and the

general absence of obligations on investors,[811] their scholarly work generally lacks explanations on how such soft law can have a determinative impact within international investment law.[812]

I will build on the analysis in Chapter 3 to explain how soft law norms, which are developed through constant interaction among States and non-state actors, are recognized as transnationalized customary international law. And, as such, if this transnationalized customary international law deals with the same subject-matter as an investment treaty without actual inconsistency between the treaty and the custom, it is justifiable to treat it as relevant and applicable liability law in ISDS tribunals. My upcoming analysis of the UNGC elaborates how ISDS tribunals can treat transnational self-regulated norms as substantive law if they a) are categorized as rules of international law (law), b) dealing with the same subject-matter as that of investment treaties (relevant), and c) imposing direct international obligations on foreign investors (applicable). The case study on the UNGC will scrutinize these criteria in detail to determine if the UNGC can be recognized as liability law in ISDS tribunals and can then be invoked by host States via the post-establishment illegality defence. This examination not only deepens our understanding of how transnational self-regulated norms might be integrated into international investment disputes but also offers a promising avenue for rebalancing the scales between investment protection and environmental accountability.

4.3 The United Nations Global Compact

In my research, the centrality of the issue of whether transnational soft law norms can be hardened into binding liability law—transnationalized customary international law—to help resolve investment disputes is elucidated by three primary developments. First, there has been a significant rise in the number of ISDS cases involving foreign investors challenging host States' regulatory measures implemented for environmental protection. Second, there is a growing trend in the development of soft norms through interactions among States and non-state actors, which expand foreign investors' obligations in areas such as sustainable development and, particularly, environmental protection. Third, there is an increasing, albeit still embryonic, reference to self-

[811] Marcoux, *supra* note 764.
[812] Andrea K Bjorklund, "Assessing the Effectiveness of Soft Law Instruments in International Investment Law" in Andrea K Bjorklund & August Reinisch, eds, *International Investment Law and Soft Law* (Edward Elgar, 2012); Jacob & Schill, *supra* note 570.

regulated norms as substantive law in ISDS tribunals to resolve the merits of investment disputes and hold foreign investors accountable at the international level.[813]

Expanding on the third reason, as these self-regulated norms gain influence, ISDS tribunals appear to be increasingly likely to incorporate them into their assessments and accordingly increasing the potential for investor rights to be balanced against their environmental obligations. This evolution not only challenges the traditional, state-centric model of international investment law but also fosters a more holistic legal environment that is more responsive to the complex challenges of our time than traditional formally determined law is capable of. For instance, in the context of (and, in significant part, spurred by) the *Urbaser* case, transnational self-regulated norms—again, often referred to as soft law—such as those encapsulated in the UNGC have been discussed as potential tools for holding foreign investors accountable in ISDS tribunals.[814] Although the UNGC initially developed as a voluntary strands and still might not be treated as legally binding on a traditional juristic basis, my contention in this dissertation is that its principles establish widely recognized transnationalized customary international law for corporate behavior, particularly regarding environmental protection and human rights. In this case, the tribunal—and commentators following it—agree. The case has opened the door to an integrated approach where soft law is not seen merely as aspirational, even as not all commentators have gone the next step to analyze clearly whether and how that "soft law" is law in a fuller sense. By this next step, when an investor's actions fall short of the internationally recognized standards set forth in instruments like the UNGC, this failure can be interpreted as a breach of a direct legal obligations on corporate investors. Consequently, host States can use these self-regulated norms for their plea of post-establishment illegality defence and then even as a basis for counterclaims, arguing that investor protections under IIAs should not preclude accountability for significant environmental or human rights violations.

In this context, I intend to doctrinally and theoretically examine whether the UNGC, particularly its environmental requirements that are primarily found in principles 7, 8, and 9, could be referred to by host States as liability law in their post-establishment illegality defence for the

[813] Marcoux, *supra* note 764.
[814] For recent studies of the role of substantive soft law in international investment law and arbitration, see *Ibid*; Adinolfi, *supra* note 543.

allegation of foreign investors' violation of international environmental law. In other words, I investigate under what conditions the UNGC could be fed into a post-establishment illegality defence in order to provide justification or excuse for host States' conduct as a response to foreign investors' non-compliance with international environmental obligations, which otherwise appears to be contrary to investment protection provisions included in IIAs. The discussion on post-establishment illegality established that, to have a successful defensive argument for holding foreign investors environmentally accountable in ISDS tribunals, host States must invoke soft law (liability law) that is both *relevant* and *applicable* to decide about the substantive aspects of investment disputes. This lays the foundations for the question that the following paragraphs are preoccupied with: Can (and, then, does) the UNGC impose environmental obligations on foreign investors that can be invoked by host States as liability law and then be determined by ISDS tribunals as relevant and applicable law to resolve the substantive aspects of investment disputes?

4.3.1 Significance of the UNGC

Amidst rising global awareness of environmental and social issues, the number of sustainability initiatives aimed at enhancing the socio-environmental responsibilities of transnational corporations has grown significantly.[815] Among these, the UNGC is the world's largest corporate sustainability responsibility initiative that seeks the consensus of the international community on the most topical issues. Announced in 1999 by former UN Secretary-General Kofi Annan and officially launched in 2000, the UNGC was established at a time when critics argued that economic globalization was insufficiently regulated and that multinational corporations were not adequately addressing the adverse social and environmental impacts of their activities.[816] Kofi Annan famously urged corporations to act in "enlightened self-interest," emphasizing that sustainable business practices could mitigate growing economic disparities and environmental degradation. By promoting the idea that corporations should act in "enlightened self-interest," the UNGC argues that sustainable practices are not only beneficial for society and the environment

[815] John Gerard Ruggie, "global_governance.net: The Global Compact as Learning Network" in Kurt Mills & Kendall Stiles, eds, *Understanding Global Cooperation: Twenty-Five Years of Research on Global Governance* (Brill | Nijhoff, 2021) 139.
[816] Alwyn Lim, "Nonprofits as socially responsible actors: Neoliberalism, institutional structures, and empowerment in the United Nations Global Compact" (2022) 70:3 Current Sociology 454–471 at 458.

but also for the long-term viability and competitiveness of businesses.[817] It can be seen from the foregoing overview that speaking of self-regulation of corporations and of the UNGC as a corporate-actor document is insufficient: consistent with both hybrid and interactional theory discussed in Chapter 3, state power is very much in the picture in the immediate form of the UN as the nurturer of the initiative and in the more diffuse form of States paying much attention to, and being themselves involved in, the process of elaborating the UNGC norms.

The UNGC is, thus, categorized as a self-regulatory guideline for accelerating the positive global impact of business for sustainable development. The UNGC emerged as a pivotal initiative in the temporal evolution of sustainable development, marking a significant shift in how sustainability principles were operationalized at the global level.[818] While early formulations of sustainable development—such as the Brundtland Report (1987)—focused primarily on the interdependence of economic growth, environmental protection, and social equity at a fairly abstract level, the UNGC (launched in 2000) translated and concretized these broad goals into voluntary corporate commitments, aiming to embed sustainability into global business practices. As a practical guideline for sustainable development, the UNGC has evolved in tandem with global sustainability agendas, particularly through its alignment with the later SDGs articulated in 2015 in the *2030 Agenda for Sustainable Development*.[819]

SDGs provide a powerful aspiration for where the UNGC's participants collectively need to go and how to get there. The integral role of the SDGs within the UNGC framework is highlighted in the UNGC's website: "The multi-year strategy of the UN Global Compact is to drive business awareness in support of achieving the Sustainable Development Goals by 2030."[820] The UNGC's mission is to "[a]ccelerate and scale the global collective impact of business by upholding the Ten Principles and delivering the SDGs through accountable companies and ecosystems that

[817] Jingjing Huang, "Corporate Social Responsibility and Financial Performance: The moderating role of the Turnover of Local Officials" (2022) 46 Finance Research Letters 102497, using a large panel of Chinese listed companies from 2010 to 2018, the study finds that complying with corporate social responsibilities, such as environmental protection efforts, positively impacts corporate financial performance, with this effect amplified particularly in non-state-owned firms.
[818] See Chapter 1 for the temporal evolution of the concept of sustainable development.
[819] Andreas Rasche, "The United Nations Global Compact and the Sustainable Development Goals" in Oliver Laasch et al, eds, *Research Handbook of Responsible Management* (Edward Elgar Publishing, 2020).
[820] "Making Global Goals Local Business | UN Global Compact", online: <https://unglobalcompact.org/sdgs>.

enable change."[821] For businesses wanting to advance the SDG agenda, the job starts by "incorporating the Ten Principles of the UN Global Compact widely into strategies and operations, and understanding that good practices or innovation in one area cannot make up for doing harm in another."[822] In this context, the UNGC serves as a guiding framework, urging participants to prioritize responsible practices and reflects a maturation of the sustainable development discourse: from high-level policy frameworks to norm-driven, participatory governance mechanisms involving private sector actors.[823] An overall point to bear in mind is that, despite the fact the UNGC's principles were textually set out at the turn of the millennium, they are not written in stone—the UNGC as a process has made clear that the meaning of those principles evolves with the later-in-time SDGs.

By promoting ten principles across human rights, labor, environment, and anti-corruption, and positioning businesses as critical partners in achieving the SDGs, the UNGC illustrates how the sustainable development paradigm—which began before the UNGC principles were expressed and continued with new normative articulations afterward—has expanded to include corporate responsibility and transnational norm diffusion as integral components of global sustainability governance. That is, the UNGC is inextricably embedded in an overall evolving normative universe of sustainable development, such that the principles must be understood in light of both what came before and what has come (and continues to come) after. The core focus of the UNGC is on accountable companies who voluntarily incorporate a set of sustainability principles into their strategies, policies, and procedures, and also establish a culture of integrity to uphold their basic responsibilities to people and planet. The UNGC principles—as informed by the SDGs—are not presented first and foremost on their surface or qua the UNGC instrument itself (versus the process that preceded, included and followed the instrument), as legally binding but rather serve as a self-regulatory framework that encourages businesses to integrate sustainability into their strategies, policies, and operational practices. A report called *The UN Global Compact Ten Principles and the Sustainable Development Goals: Connecting, Crucially,* released by the UNGC in 2016, argues that, "as the world's largest corporate sustainability initiative, anchored in

[821] "Our Mission | UN Global Compact", online: <https://unglobalcompact.org/what-is-gc/mission>.
[822] "The SDGs Explained for Business | UN Global Compact", online: <https://unglobalcompact.org/sdgs/about>.
[823] United Nations Global Compact (UNGC), *UN Global Compact 2022 Annual Report* (2023), online: <https://globalcompact.at/wp-content/uploads/2023/04/UN-GLOBAL-COMPACT_2022-ANNUAL-REPORT.pdf>.

the United Nations and encompassing UN principles and values, the UN Global Compact is uniquely poised to become the world's most relevant business-oriented initiative in relation to the attainment of the SDGs."[824] The report emphasizes that "the UN Global Compact Ten Principles are the foundation for any company seeking to advance the SDGs." By incorporating the UNGC's principles into strategies, policies, and procedures, participants are not only upholding their basic responsibilities to the society and environment, by setting the stage for their long-term economic success but doing so by treating the UNGC' Principles as inextricably connected to the SDGs.

The UNGC was developed to establish a global consensus on the rapid integration of the economy, which has led to the expansion of transnational corporations' influence across borders, resulting in transboundary socio-environmental externalities. The UNGC was a response to this concern, aiming to ensure that economic progress did not compromise human rights, fair labor practices, environmental sustainability, or ethical governance. By focusing on these four thematic areas, the UNGC provided a unique platform that brought together diverse actors, including the private sector, States, and civil society. This collaborative dialogue was crucial in developing shared ethical standards that could guide corporate conduct globally through its ten general principles. The UNGC's Ten Principles served as a common language for these stakeholders, facilitating discussions about best practices and setting expectations that transcended national and cultural boundaries. See Table 1.

Table 1: The UNGC Principles.[825]

Corporate sustainability starts with a company's value system and a principles-based approach to doing business. This means operating in ways that, at a minimum, meet fundamental responsibilities in the areas of human rights, labour, environment and anti-corruption. Responsible businesses enact the same values and principles wherever they have a presence, and know that good practices in one area do not offset harm in another. By incorporating the Ten Principles of the UN Global Compact into strategies, policies and procedures, and

[824] United Nations Global Compact (UNGC), *The UN Global Compact Ten Principles and the Sustainable Development Goals: Connecting, Crucially* (2016), online: <https://d306pr3pise04h.cloudfront.net/docs/about_the_gc%2FWhite_Paper_Principles_SDGs.pdf> at 11.
[825] United Nations Global Compact (UNGC), *supra* note 5.

establishing a culture of integrity, companies are not only upholding their basic responsibilities to people and planet, but also setting the stage for long-term success.

The Ten Principles of the United Nations Global Compact are derived from: the Universal Declaration of Human Rights, the International Labour Organization's Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development, and the United Nations Convention Against Corruption.

Human rights

Principle 1: Businesses should support the protection of internationally proclaimed human rights; and

Principle 2: make sure that they are not complicit in human rights abuses.

Labour

Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining,

Principle 4: the elimination of all forms of forced and compulsory labour,

Principle 5: the effective abolition of child labour; and

Principle 6: the elimination of discrimination in respect of employment and occupation.

Environment

Principle 7: Businesses should support a precautionary approach to environmental challenges,

Principle 8: undertake initiatives to promote greater environmental responsibility; and

Principle 9: encourage the development and diffusion of environmentally friendly technologies.

Anti-corruption

Principle 10: Businesses should work against corruption in all its forms, including extortion and bribery.

By joining the UNGC, corporations commit to voluntarily incorporating these ten principles into their business models. Alongside this focus on voluntary adherence, it must be observed that the 10 principles do not expressly include a principle with respect to corporate legal liability nor does there appear to be surrounding evidence that, at the time of adopting the UNGC, corporate liability was intended to be an adjunct feature of each—or, at least, some—of the principles. Instead, apart from voluntary incorporation into corporate policies, the primary formal accountability mechanism of the UNGC is its signatories' commitment to submit an annual Communication on Progress (CoP) report, which requires companies to publicly disclose their efforts and improvements in implementing the Compact's principles. This transparency mechanism enhances corporate accountability and encourages continuous improvement—while staying silent on the implications for legal liability. This state of affairs hearkens back to the discussion in Chapter 3 of the *Nevsun* case—in terms of whether general international law (be it traditional interstate custom or transnationalized custom) requires a specific liability rule to have evolved or whether liability is instead a generalized feature of the international law of responsibility for violations of international obligations. I will return to this question, while noting at the outset that it is the latter position that I understand to be the best account of where liability comes from in international law—on the basis of the idea of liability being part of the very fabric of international law through the operation of the ICJ Statute article 38's general principles of law (whether general principles of law are understood as principles derived from commonalities across domestic legal system, as foundational principles of international law beyond States' consent and acquiescence, as a kind of repository for notions of principles inherent to legality in Fuller's sense, or a mix of some or all of these).

How does the UNGC relate, in terms of its normative content and the kinds of responsibilities it wishes corporations to assume, to the investment field with which we are concerned in this dissertation? Quite obviously, principles 7, 8 and 9 are most directly on point, although the two provisions on human rights (apart from labour rights), principles 1 and 2, may also be relevant in multiple ways due to the intersections of human rights and the environment (e.g. Indigenous rights in relation to land, health rights, rights to food and water, and so on). Focusing on

principles 7 through 9, the UNGC expects investors, employers, and producers in dozens of countries worldwide to "support a precautionary approach to environmental challenges. … undertake initiatives to promote greater environmental responsibility and … encourage the development and diffusion of environmentally friendly technologies."[826] Through these environmentally relevant requirements, the UNGC attempts to institutionalize shared global understandings of environmental protection, provide a normative framework to address the environmentally risky behavior of corporations and create a sustainable global economy that delivers lasting benefits to all people, communities, and markets.[827]

The UNGC is selected for this study both because of its subject-matter that is so closely connected to both the benefits and harms of investment activity and because, since its foundation in 2000, it has witnessed unprecedented growth for a voluntary global governance agency.[828] Compared with other initiatives, the UNGC is the world's largest corporate sustainability initiative that, as of January 2024, has more than 24,469 active participants with significant geographic reach covering more than 167 countries.[829] With the broad-based support of all 193 participant States of the UN General Assembly, the UNGC remains the single, global normative authority and reference point for action and leadership within a growing global corporate sustainability movement—this including the folding-in of the SDGs into the understanding of the content of the UNGC principles after the SDGs' arrival on the global stage in 2015. With tens of thousands of participating companies, which not only playing role in developing the UNGC but also complying with its principles, from over 160 countries, the UNGC has become a global intensity in promoting sustainable business practices.[830] The UNGC's normative influence

[826] Kofi Annan, "An appeal to world business: 31 January 1999" in Malcolm McIntosh, Sandra Waddock & Georg Kell, eds, *Learning To Talk: Corporate Citizenship and the Development of the UN Global Compact* (London: Routledge, 2004) 28 at 30.
[827] See Malcolm McIntosh, Sandra Waddock & Georg Kell, eds, *Learning to Talk: Corporate Citizenship and the Development of the UN Global Compact* (London: Routledge, 2004).
[828] Christian Voegtlin & Nicola M Pless, "Global Governance: CSR and the Role of the UN Global Compact" (2014) 122:2 Journal of Business Ethics 179–191 at 179.
[829] United Nations Global Compact (UNGC), *supra* note 5.
[830] It could reasonably be countered that wide adoption is tied—or tied to a considerable extent—to extremely vague goals. This may be conceded, but vagueness in soft law instruments can provide a broad and adaptable framework that can respond to the evolving nature of environmental challenges, allowing regulators and courts to interpret norms flexibly in light of new scientific evidence or socio-political and technological contexts. Additionally, this vagueness can help build consensus among diverse stakeholders by avoiding overly prescriptive rules, thereby strengthening normative power, promoting voluntary compliance, and laying the groundwork for future binding regulations.

extends beyond individual corporate behavior—it also shapes international agreements and encourages governments to adopt similar sustainability-oriented frameworks.[831]

Furthermore, the mission statement and objectives of the UNGC clearly indicate that it aims to achieve more than merely identifying a set of principles that corporations must adhere to (once they first voluntarily commit to them). Instead, the broader governance framework of the UNGC actively involves corporations in directing and disseminating these principles, rather than assuming that they are passive recipients of an international code of practice. This is paramount outstanding when it comes to differentiating this initiative from others at the international level. In addition, the UNGC is also special because it complements other corporate responsibility initiatives by creating an interactive platform for diverse actors to be engaged in the conversation about human rights, labour standards, and environmental protection. Indeed, it promotes dialogue on the relationship between business and society—both to develop the set of principles through which businesses and the UN can work in partnership for global development and to pursue their actualization post-adoption of the principles.

The development process of the UNGC took place initially according to the universal attention given to greater engagement of transnational corporations in extending the benefits of the globalized market economy to the billions of people suffering desperate poverty.[832] It then sped up through partnerships among States and non-state actors to collaborate in addressing a wide variety of global problems—including the extent of harm that corporate actors can cause.[833] By promoting the idea that corporations would operate not only by being profitable but also by being engaged in meaningful dialogue on human rights and environmental protection, the UNGC has taken a lead not just on talking but also on walking the talk towards the SDGs of the UN.[834] Literature on this issue shows that the UNGC has quickly become an important benchmark in the dialogue on global and corporate governance, as it enables corporations to improve social

[831] See the discussion on the Continues Practice of Legality.
[832] See Lisbeth Segerlund, *Making Corporate Social Responsibility a Global Concern: Norm Construction in a Globalizing World* (London: Routledge, 2010).
[833] James Post, "The United Nations Global Compact: A CSR Milestone" (2013) 52:1 Business & Society 53–63.
[834] McIntosh, Waddock, & Kell, *supra* note 827 at 13.

performance,[835] environmental consideration,[836] relationships with the stakeholders,[837] and attractiveness to new investors.[838]

Accordingly, the UNGC was designed not only to encapsulate a global consensus on critical issues but also to serve as a dynamic forum for multi-stakeholder engagement. By establishing shared ethical standards through its ten principles, it has played a pivotal role in guiding corporate conduct on a global scale, promoting a balanced approach to economic growth and sustainable development. The significant benefits that the UNGC brings to the adhering organizations and the network that the UNGC creates among concerned companies along with the high number of corporations registered to comply with the UNGC's environmental principles make the UNGC the ideal subject to shed light on the potential for "soft law" of corporate responsibility for sustainable development to have evolved into a source of international law, namely, transnationalized international customary law, in resolving the substantive aspects of investment disputes and upholding foreign investors environmentally accountable in ISDS tribunals. This evolving approach, if persuasively established, can expand the accountability of investors beyond traditional treaty protections, pushing them to align their operations with globally recognized sustainability standards. In what follows, I will seek to demonstrate that, in accordance with the process-based and legality approach to international custom discussed in Chapter 3, the principles of the UNGC, which have been traditionally/initially classified as "soft law"—law that is somehow not binding or binding but not enforceable by tribunals or courts—have turned into transnationalized customary international law capable of imposing international environmental obligations on investors. They can then be used in investment disputes as liability law, especially in contexts where host States invoke post-establishment illegality defence for investors' alleged violations of international law.

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[835] Eduardo Ortas, Igore Alvarez & Ainhoa Garayar, "The Environmental, Social, Governance, and Financial Performance Effects on Companies that Adopt the United Nations Global Compact" (2015) 7:2 Sustainability 1932–1959.
[836] Sabine Einwiller, Christopher Rupple & Alexandra Schnauber, "Harmonization and Differences in CSR Reporting of US and German Companies: Analyzing the Role of Global Reporting Standards and Country-of-Origin" (2016) 21:2 Corporate Communications: An International Journal.
[837] Olga Andrianova & Taisiya Yeletskikh, "Societal marketing: Integration of European Experiences into Business Practices in Belarus" (2012) 7:2 International Journal of Emerging Markets 107–131.
[838] Michel Coulmont & Sylvie Berthelot, "The Financial Benefits of a Firm's Affiliation with the UN Global Compact" (2014) 24:2 Business Ethics, The Environment and Responsibility.

4.3.2 Emergence of the UNGC

In the 1970s, following the historical resistance to corporate responsibility that characterized multinational business practices, several political scandals heightened public intolerance of corporate misconduct and underscored the evolution of corporate responsibility policies.[839] These scandals, which ranged from corruption cases to environmental disasters, underscored the urgent need for a more structured approach to corporate accountability.[840] This shift marked the beginning of the evolution of corporate responsibility policies, as governments, international organizations, and civil society increasingly pressured businesses to adopt ethical and socially responsible practices. In this context, with the purpose of engaging the private sector to better communicate the value of the UN to the business community[841] and also responding to numerous social movements around the world putting pressure on companies demanding responsible behavior towards socio-environmental issues,[842] between 1998 and 1999, a series of meetings were convened by the International Chamber of Commerce (ICC). The meetings of the ICC, a global business association that had long embraced multilateralism and the promotion of investment, were intended to bridge connecting common interests across national boundaries by noting that investment activities of transnational corporations must be seen as a vehicle for generating shared prosperity, interdependence, and peace.[843] These meetings served as a platform for dialogue between public and private actors, with the goal of aligning corporate interests with the broader objectives of sustainable development. [844] The ICC, recognizing the growing importance of corporate responsibility in an interconnected global economy, convened global business leaders to discuss transnational corporate investment with the focus on shared prosperity, interdependence, and peace. During these discussions, the business community—

[839] Post, "The United Nations Global Compact", *supra* note 833 at 55.
[840] See David Vogel, *The Market for Virtue: The Potential and Limits of Corporate Social Responsibility* (Brookings Institution Press, 2005). This book provides a historical overview of corporate scandals and how they contributed to the rise of corporate social responsibility (CSR).
[841] Annan, *supra* note 826.
[842] Luis A Perez-Batres et al, "Stakeholder Pressures as Determinants of CSR Strategic Choice: Why do Firms Choose Symbolic Versus Substantive Self-Regulatory Codes of Conduct?" (2012) 110:2 Sustaining Sustainability in Organizations 157–172.
[843] Georg Kell, "The Global Compact Selected Experiences and Reflections" (2005) 59:1 Journal of Business Ethics 69–79.
[844] United Nations Meetings Coverage and Press Releases, *United Nations and International Chamber of Commerce to Cooperate on Project to Stimulate Investment Flows to Africa and Least Developed Countries* (1998), online: <https://press.un.org/en/1998/19980209.sg2042.html>.

represented by the ICC—acknowledged that investment activities of transnational corporations must be seen not just as profit-driven ventures but as a means to foster shared prosperity, economic interdependence, and global peace. This perspective marked a crucial turning point in the corporate responsibility movement, as it reinforced the notion that businesses could no longer operate in isolation from broader societal and environmental concerns. Instead, they had to engage in ethical business practices that contribute to long-term sustainability and stability.

As a result of such negotiations, in 1999, the *Davos Speech* was delivered by former UN Secretary-General Kofi Annan, who introduced the UNGC and pointed out the UN partnership with the business community in achieving sustainable development goals: "You, the business leaders gathered in Davos, and we, the United Nations, initiate a global compact of shared values and principles, which will give a human face to the global market." The *Davos Speech* introduced the UNGC as the world's largest network-based voluntary corporate responsibility initiative, supported by the moral legitimacy and the political backing of the UN and aimed at enhancing cooperation among a diverse set of actors. In 2000, ICC endorsed the UNGC, aligning with its 10 principles on human rights, labor, environment, and anti-corruption in order to promote corporate participation in global governance efforts. The initiative sought to bridge the gap between corporate interests and global governance (especially as understood as primarily an interstate affair), emphasizing that responsible business conduct was not only a moral imperative but also essential for maintaining trust, stability, and long-term economic success in an increasingly interconnected world.[845]

As a voluntary initiative, the UNGC "has explicitly adopted a learning approach to inducing corporate change, as opposed to a regulatory approach; and it comprises a network form of organisation, as opposed to the traditional hierarchic/bureaucratic form."[846] Here, "regulatory" means that the principles of the UNGC are not imposed through strict, top-down regulations. Instead, they are cultivated through ongoing interaction, collaboration, and mutual learning

[845] Andreas Rasche, Sandra Waddock & Malcolm McIntosh with the collaboration of Andreas Rasche, Malcolm McIntosh & Sandra Waddock, "The United Nations Global Compact: Retrospect and Prospect" (2013) 52:1 Business & Society 6–30.
[846] John Gerard Ruggie, "The Theory and Practice of Learning Networks: Corporate Social Responsibility and the Global Compac" in Malcolm McIntosh, Sandra Waddock & Georg Kell, eds, *Learning to Talk Corporate Citizenship and the Development of the UN Global Compact* (London: Routledge, 2004) 32 at 33.

among participants: "governments, who defined the principles on which the initiative is based; companies, whose behaviour the Global Compact seeks to shape; labour, in whose hands the concrete process of global production takes place; NGOs, representing the wider community of stakeholders; and the United Nations, the world's only truly global political entity."[847] Based on its principles—as noted earlier, derived from the Universal Declaration of Human Rights,[848] the International Labour Organization's Declaration on Fundamental Principles and Rights at Work,[849] the Rio Declaration on Environment and Development,[850] and the the United Nations Convention Against Corruption[851] and then supplemented by the arrival of the SDGs—the UNGC seeks to engage the private sector to collaborate with the UN to address issues concerning human rights, labour, environment, and anti-corruption.[852] This network-based structure allows for flexible engagement and encourages companies to internalize and progressively implement responsible practices. The development of the principles, therefore, evolves organically through shared experiences and best practices—rather than being rigidly dictated by a central authority—in order to weave the principles into global corporate practice by bringing together all the relevant social actors.

The UNGC has shifted the relationship between the UN system and the business sector in two ways. First, the UN went beyond the dominant approach of dealing with the impact of transnational corporations from a belief in solutions based solely on interstate regulation. Instead, it considered a more flexible approach involving business entities and States in addressing global issues.[853] Because of its initial focus on transnational corporations within a globalized neoliberal culture, the UNGC framework emphasizes organizational autonomous responsibility as the outgrowth of businesses lobbying for less state-centric regulation in favor of voluntary efforts to

[847] *Ibid* at 42.
[848] United Nations, *supra* note 283.
[849] International Labour Organization (ILO), *ILO Declaration on Fundamental Principles and Rights at Work and its Follow-up* (1998), online: <https://www.ilo.org/sites/default/files/2024-04/ILO_1998_Declaration_EN.pdf>.
[850] United Nations, *The Rio Declaration on Environment and Development,* (1992), online: <https://www.un.org/en/development/desa/population/migration/generalassembly/docs/globalcompact/A_CONF.151_26_Vol.I_Declaration.pdf>.
[851] *The United Nations Convention against Corruption, 2349 U.N.T.S. 41, 31 October 2003 (entered into force 14 December 2005)*, online: <https://www.unodc.org/documents/treaties/UNCAC/Publications/Convention/08-50026_E.pdf>.
[852] United Nations Global Compact (UNGC), *supra* note 5.
[853] Jennifer Bair, "From the Politics of Development to the Challenges of Globalization" in *Recognition and Redistribution* (London: Routledge, 2009).

improve their social and environmental practices while having more freedom from government regulation.[854] Second, adopting a less state-centered approach also changed the nature of UN-business relations from a largely confrontational/reactive attitude toward a more collaborative/proactive one.[855] Cultural changes arising from the globalized market economy made it more legitimate for the UNGC to be established based on collective action and collaboration among States and transnational corporations that embraced counterpart responsibility for tackling global social and environmental issues.[856]

This dynamic is further clarified by Georg Kell, former executive head of the UNGC, who remarks that the governance of the UNGC provides a decentralized and flexible framework according to which, "instead of a command-and-control type of governance, in which decisions are pushed down for implementation, the voluntary and demand-driven nature of the UN Global Compact implies that changes require the buy-in of participants."[857] Although the UNGC is often seen as the emergence of private authority in global governance, "governments are intimately involved, by providing policy space for the initiative within the intergovernmental framework of the UN and by offering funding and other means of direct support."[858] It, therefore, "is a mix of public and private authority whose legitimacy is neither mandated nor assured" and collaboration among the business sector and States is motivated by shared incentives rather than hierarchical order.[859] Kell also explains that the conviction underlying the voluntary nature of the UNGC is that businesses have a self-interest in working toward sustainable markets and long-term economic stability and, as a result, willingly make positive contributions to the UN agenda of sustainable development. He argues that organizational responsibilities, such as environmental commitments, are driven by "micro-economic imperatives essential for corporate survival."[860] It means that corporate and organizational success requires, for instance, stable economies along with skilled workers, which can be achieved by adopting the UNGC's principles. Based on

[854] Daniel Kinderman, "Free us up so we can be responsible!' The co-evolution of Corporate Social Responsibility and neo-liberalism in the UK, 1977–2010" (2012) 10:1 Socio-Economic Review 29–57.
[855] Rasche, Waddock & McIntosh, "The United Nations Global Compact", *supra* note 845.
[856] Georg Kell & David Levin, "The Global Compact Network: An Historic Experiment in Learning and Action" (2003) 108 Business and Society Review 151–181.
[857] Georg Kell, "12 Years Later: Reflections on the Growth of the UN Global Compact" (2013) 52:1 Business & Society 31–52 at 43.
[858] Kell, *supra* note 843 at 24.
[859] *Ibid* at 75.
[860] *Ibid* at 74.

shared values and mutual benefits, the UNGC helps transnational companies internalize socio-environmental principles so that they can shape and reshape corporate practices as external conditions change.[861]

The environmental principles articulated by the UNGC, the voluntary nature of the UNGC, and the fundamental changes the UNGC brings in the relationship between States and non-state actors encourage me to examine the role that the UNGC could play at the transnational level, particularly within investor-state dispute settlement tribunals.[862] The non-binding structure of the UNGC is of paramount relevance to the topic of my study, which investigates whether self-regulated norms can be considered substantive law to hold foreign investors accountable in ISDS tribunals.

In seeking to conceptualize the role that the UNGC plays in global environmental governance and then in resolving investor-state disputes, I must, as made clear several times to this point, examine the *relevance* and *applicability* of the UNGC in resolving the substantive aspects of investment disputes. In so doing, first, I study the environmental principles of the UNGC in light of two criteria—their subject-matter correspondence and (in)consistency among their requirements with investment agreements—to know whether the UNGC is *relevant* to resolving investment disputes. Second, I discuss the legal status of the UNGC as a source of international law to determine its *applicability* to investment disputes, notably as a generator of direct legal obligations on investors. With this object in mind, I will apply the transnational legal pluralism, hybridity and interactional theory discussed in Chapter 3, which interrelatedly explain the participatory role of non-state actors in the lawmaking process and examine the legitimacy of non-state-based norms, to consider the UNGC as transnationalized international customary law capable of imposing environmental obligations on foreign investors and holding them environmentally accountable in ISDS tribunals.

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[861] Ruggie, *supra* note 846.
[862] Michele M B Btsill & Harriet Bulkeley, "Cities and the Multilevel Governance of Global Climate Change" in Kurt Mills & Kendall Stiles, eds, *Understanding Global Cooperation: Twenty-Five Years of Research on Global Governance* (Brill | Nijhoff, 2021) 219.

4.3.3 Relevance of the UNGC for Investment Treaty Interpretation

Interactions between investment treaties and the UNGC should be managed in accordance with Article 31(3)(c) of VCLT, introducing systemic interpretation to harmonize rules of international law. As discussed in Chapter 2, to better reflect the legal subjects' general intent and to better account for the context in which investment treaties are developed, investment arbitrators should interpret the treaties against the background of "relevant rules of international law." To assess whether the environmental principles of the UNGC could be assumed *relevant* by ISDS tribunals in treaty interpretation, there are two consequential criteria to be considered: sameness of the subject-matter of investment treaty and that of the UNGC and consistency among investment treaty' rules and the UNGC's principles.

4.3.3.1 Sameness of Subject-Matter

The first step for determining the relevance of the UNGC as liability law is to identify whether investment treaty and the UNGC's principles correspond with the same subject-matter. By recalling the functional perspective discussed earlier, a "moderate" approach on sameness of the subject-matter—a middle position between conceptually and linguistically narrow focus on subject-matter labels, on the one hand, and broad assertions that ultimately all custom is relevant to all treaties because everything must be understood to cohere and systemically hold together—requires the consideration of: object and purpose, context and topic, and value compatibility.

Object and purpose, which illuminate the normative goals and functional roles each rule is intended to serve, are integral in assessing the sameness of two rules of international law.[863] The object of a treaty is "the instrument for the achievement of the treaty's purpose, and this purpose is, in turn, the general result which the [P]arties want to achieve by the treaty."[864] To further elaborate on the functional perspective, "context and topic" should be also taken into consideration in order to realize if treaty law and customary law have the same subject-matter. In

[863] Sands, *supra* note 459; Cordonier Segger, *supra* note 7.
[864] Richard K Gardiner, *Treaty interpretation*, second edition ed (Oxford, United Kingdom; New York, NY: Oxford University Press, 2015) at 213.

this perspective, sameness of subject-matter means that even if legal norms originate from different fields or regimes (e.g., investment law vs. environmental law), they can still be considered part of the same subject-matter if they serve similar regulatory goals and policy concerns or are coherent enough *inter se* that they cannot be separated. "Value compatibility" is also of paramount in determining sameness of subject-matter as it refers to the idea that both legal regimes reflect or promote compatible underlying values. Suppose an investment treaty promotes non-discriminatory treatment of investors and CIL also upholds due process. Even they arise in different domains (investment law vs. human rights law), if they both protect against unfair treatment, they might be seen as expressing a compatible value and thus as supporting mutual integration or reinforcement. Accordingly, considering these factors helps determine whether treaty law and CIL are directed toward the same subject-matter—essential for evaluating whether systemic interpretation could be used for harmonization. All these finer distinctions notwithstanding, it should also be noted that case law and commentary often discuss relevance as sameness in quite loose ways where overlaps between subject-matter and purposes is very common.

The object and purpose of the UNGC are centered on fostering SDGs by promoting corporate social responsibility, environmental protection, human rights, labor rights, and anti-corruption measures. The UNGC establishes a framework through which businesses voluntarily align their operations and strategies with these universal principles, emphasizing the role of the private sector in advancing global sustainability. Similarly, investment treaties are primarily designed to ensure legal certainty and stability for foreign investors within a broader objective of encouraging FDI as a driver of sustainable economic growth, technological advancement, social progress, and environmental sustainability in host countries. By providing protections such as fair and equitable treatment, protection against expropriation, and non-discriminatory treatment, investment treaties seek to create an enabling environment for investment that contributes to economic and social development. In particular, the UNGC's principles 7, 8, and 9 consider the environmental obligations of businesses in relation to a precautionary approach, environmental responsibility, and development and diffusion of environmentally friendly technologies. Combining these three sets of obligations, the UNGC requires businesses, particularly leading transnational corporations, to recognize the link between environmental issues and development

priorities by acting in environmentally responsible ways concerning climate change, water and sanitation, energy, biodiversity, and food and agriculture.

One must acknowledge that the aim of investment treaties is often articulated in considerably narrower terms, as something like "help[ing] establish an investment climate that will attract foreign investment and encourage its establishment in the host economy and to protect outward investors in foreign markets."[865] However, at no instance has the UN General Assembly (UNGA) suggested that developing countries should allow investment treaties to limit the effective implementation of environmental and social accords or that corporations should expect, far less demand for social and environmental consideration. Taking the UN's Agenda 21 (now over a quarter-century old) as a leading example of integration of investment-related and environmentally-related subject matter within overarching shared purposes, States should have "a balanced and integrated approach to trade and sustainable development, based on a combination of trade liberalization, economic development and environmental protection."[866] Consistent with the baseline normative role of Agenda 21, it has further been proposed that sustainable development is best characterized as the object and purpose of a wide range of international treaties.[867]

Legal scholars, such as Cordonier Segger—who is an expert in the fields of sustainable development and responsible investment—highlights in her recent publication, *Crafting Trade and Investment Accords for Sustainable Development*, that "States accept sustainable development as part of the 'object and purpose' of trade and investment treaties."[868] She notes that sustainable development is increasingly being recognized not just as a peripheral or aspirational idea but as a core goal of investment agreements. When States negotiate and enter into treaties, especially in the area of investment, they now often explicitly or implicitly include language or provisions that reflect a commitment to sustainable development. As such, recent

[865] Jansen Calamita, *Handbook on Obligations in International Investment Treaties* (2020), online: <https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/apec_handbook_on_obligations_in_iit.pdf>.
[866] para 29.
[867] Alan Boyle & David Freestone, eds, *International Law and Sustainable Development: Past Achievements and Future Challenges* (Oxford University Press, 1999).
[868] Cordonier Segger, *supra* note 7 at 27.

trends in investment treaty-making negotiation "take place against a backdrop of broader international policy debates in which States have not been silent on linkages with environmental, human rights, and sustainable development considerations."[869] To explain how sustainable development is increasingly and explicitly mentioned in investment treaties, Newcome notes, between 2000-2005, a limited number of investment treaties subtly refer to sustainable development.[870] For instance, Mozambique-Netherlands investment treaty requires state parties to achieve the treaty's objectives "without relaxing health, safety and environmental measures of general application."[871] However, since then, emerging free trade agreements and multilateral agreements with investment protection provisions contain more express references to sustainable development.[872] For example, the India-Singapore CECA includes in its preamble that "economic and trade liberalisation should allow for the optimal use of natural resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment."[873] Likewise, Ruse-Khan admits that numerous "international, regional and bilateral trade agreements already contain sustainable development as their object and purpose."[874] He also explains that sustainable development is explicitly recognized as part of the

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[869] Marie-Claire Cordonier Segger, "Inspiration for Integration: Interpreting International Trade and Investment Accords for Sustainable Development" (2017) 3:1 Canadian Journal of Comparative and Contemporary Law at 165. I am treating 2017 as comparatively recent, but acknowledge that even eight years is enough time for trends to slow and reverse. Careful observers of the landscape have commented to me that the trend may now be turning around. There is not much that can be said if this turns out to be true, other than that regression can itself be turned back and the previous trends picked up again. This point is also emphasized in Hongwei Dang, *Sustainable Development in International Investment Law: Treaties and Arbitral Practice* (Doctoral Thesis, Erasmus University Rotterdam, 2022) at 34:

> There is a clear trend for increasing frequency in the inclusion of sustainable development concerns. Since 2010, every year at least half of the newly signed BITs incorporate SDPs [Sustainable Development Provisions], and this rate goes up to more than 75% from 2013, maintaining the high level from then. Over time, not only is the general quantity of BITs with SDPs becoming progressively higher, but also the number of provisions in BITs which relate to sustainable development is increasing and these provisions are more diverse too. In other words, more recently signed treaties tend to introduce more diverse sustainable development factors such as environment, human rights, anti-corruption in various preambular, substantive or procedural provisions.

[870] Newcombe, *supra* note 17.

[871] *Agreement between the Government of the Republic of Mozambique and the Government of the Kingdom of the Netherlands Concerning the Encouragement and the Reciprocal Protection of Investments (2001)*, online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2055/download>.

[872] Newcombe, *supra* note 17.

[873] *Comprehensive Economic Cooperation Agreement between The Republic of India and the Republic of Singapore, India- Singapore CECA (2005)*, online: <https://www.eicindia.gov.in/WebApp1/resources/PDF/FTA_CECA_Agreement.pdf>.

[874] Henning Grosse Ruse-Khan, "A Real Partnership for Development? Sustainable Development as Treaty Objective in European Economic Agreement Partnerships and beyond" Google Scholar (2010) 13:1 Journal of international economic law 139–180 at 142.

object and purpose of emerging investment treaties. As far back as 2006, in the context of the EU entering into investment agreements, Pallemaerts was pointing out that sustainable development is one of the overriding objectives of investment treaties.[875] It means that, for a considerable time now but also especially in recent years, sustainable development is not merely a peripheral concern but is embedded as a core value in these agreements.

More specifically, many countries now seek to expressly promote sustainable development in the new free trade or international investment agreements they negotiate rather than relying on sustainable development as an implicit (even if still clear) objective. For example, the European Community is currently negotiating investment treaties called Economic Partnership Agreements (EPAs). Among these agreements, EC – CARIFORUM EPA (CEPA) considers itself a "Trade Partnership for Sustainable Development"[876]—emphasizing that the overarching objective is sustainable development of the parties to the partnership.[877] The EC Commission also describes CEPA as "a new kind of free-trade agreement as sustainable development is the presiding principle governing the whole agreement."[878] That was 20 years ago, and there was already linkage between sustainable development in authoritative textual locations a decade before that. For example, the Treaty of the European Union, as amended by the Treaty of Amsterdam, recognizes "the following objectives:…to achieve balanced and sustainable development."[879] The preamble of the WTO Agreement, negotiated in the 1996 Singapore Ministerial Declaration, also states that "[f]ull implementation of the WTO Agreements will make an important contribution to achieving the objectives of sustainable development."[880] The WTO Appellate Body in the 1998 US–Shrimp case had already acknowledged that: "the preamble of the WTO

[875] Marc Pallemaerts, "The EU and Sustainable Development: An Ambiguous Relationship" in Marc Pallemaerts & Albena Azmanova, eds, *The European Union and Sustainable Development: Internal and External Dimensions* (Brussels: VUB Press, 2006).
[876] See the heading of Part I of the EC – CARFORUM which contains the objectives and principles of the agreement, European Community & CARIFORUM States, *Economic Partnership Agreement between the CARIFORUM States, of the one part, and the European Community and its Member States, of the other part* (2008), online: <https://www.consilium.europa.eu/en/documents/treaties-agreements/agreement/?id=2008034>.
[877] European Community & CARIFORUM States, *Economic Partnership Agreement between the CARIFORUM States, of the one part, and the European Community and its Member States, of the other part* (2008), online: <https://www.consilium.europa.eu/en/documents/treaties-agreements/agreement/?id=2008034> Article 1(a) and 3.
[878] *Ibid* at 3.
[879] at 7.
[880] World Trade Organization (WTO), *Singapore Ministerial Declaration (18 December 1996) WT/MIN(96)/DEC, 36 ILM 218*, online: <https://www.wto.org/english/thewto_e/minist_e/min96_e/wtodec_e.htm>.

Agreement...explicitly acknowledges 'the objective of sustainable development'."[881] The tribunal further clarified in the corresponding footnote that "[t]his concept has been generally accepted as integrating economic and social development and environmental protection."[882] Furthermore, WTO members in the 2001 WTO Doha Declaration also reiterated that "[w]e strongly reaffirm our commitment to the objective of sustainable development" and further clarified that "[w]e are convinced that the aims of upholding and safeguarding an open and non-discriminatory multilateral trading system, and acting for…the promotion of sustainable development can and must be mutually supportive."[883]

Furthermore, such inclusion is not limited to the sustainable development concept. Some investment treaties expressly refer to the UNGC as a means of achieving sustainable development. For example, the model treaty elaborated by Austria mentions that the contracting parties "TAK[E] NOTE OF the principles of the UN Global Compact."[884] The Free Trade Agreement Between the EFTA States and Montenegro also requires the parties to acknowledge good corporate governance and corporate social responsibility for sustainable development by observing "[i]nternationally recognized guidelines and principles in this respect, such as the OECD Guidelines for Multinational Enterprises, the OECD Principles of Corporate Governance and the UN Global Compact."[885] In these references, the object and purpose of the international trade and investment regimes are linked to sustainable development purposes rather than only boosting economic growth. A comprehensive list of treaties could be seen in the following discussion on "Continuous practice of legality."

In conclusion, from the functional viewpoint, both the UNGC and investment treaties aim to achieve sustainable transnational economic activity. Specifically, the UNGC advances principles such as human rights and environmental protection—not to restrict business, but to make global

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[881] *United States: Import Prohibition of Certain Shrimp and Shrimp Products,* WT/DS58/AB/R, Report of the Appellate Body 12 October 1998.
[882] *supra* note 881 para 129.
[883] World Trade Organization (WTO), *Doha WTO Ministerial 2001: Ministerial Declaration, WT/MIN(01)/DEC/1* para 6.
[884] *Agreement for the Promotion and Protection of Investment between the Republic of Austria and ___* (2008), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/4770/download>.
[885] *Free Trade Agreement Between the EFTA States and Montenegro* (2012), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/2622/download> at IV.

markets more inclusive and sustainable. Investment treaties also seek to encourage cross-border investment flows, while achieving sustainable development simultaneously—not to undermine the environment, but to make global markets more inclusive and sustainable. These purposes are *coherent* and *overlapping* rather than contrasting. Contextually, both frameworks have been influenced by the growing recognition of corporate accountability and the integration of environmental concerns into international economic governance. For instance, arbitral jurisprudence increasingly acknowledges environmental protection when balancing state regulatory space with investor rights and discussing investors' obligations—illustrating practical convergence in their fields of application. From a value compatibility standpoint, both regimes promote sustainability.[886] The growing number of investment treaties' preambles and provisions on environmentally responsible investments and the UNGC's principle on environmental consideration both reflect a shared value for sustainable development. Therefore, even though investment treaties and the UNGC might be assumed to be located in fragmented fields or regimes of international law, they are not. Accordingly, they have to be systemically interpreted to harmonize norms between the two, rather than treating them as operating in isolation.

4.3.3.2 Consistency

The second step in determining the relevance of the UNGC as liability law is to determine consistency among investment treaty and the UNGC's environmental principles. Consistency is a legal idea that refers to the absence of actual conflict (an actor can comply with both sets of obligations). As discussed before, investment treaties can seek in some way to either reflect, build

[886] Although the concept of sustainable development is increasingly embedded in policy frameworks at national and international levels, it continues to face criticism for its conceptual vagueness and limited practical enforceability. Critical environmental law scholars also argue that the concept of sustainable development is vague and elusive because it lacks a universally accepted definition and is used inconsistently across legal systems, sectors, and regions. This vagueness could limit its practical effectiveness and create challenges for implementation and enforcement within international environmental law—especially if the overarching concept of "sustainable development" is what is invoked versus invoking more concrete normative development in relation to a given SDG (or aspect of a given SDG). See Evgenia Pavlovskaia, "Are We There Yet? A Legal Assessment and Review of the Concept of Sustainable Development under International Law" (2013) 2:1 Journal of Sustainable Development Law and Policy 139–152; Alan E Boyle, "The Gabcikovo-Nagymaros Case: New law in old bottles" (1997) 8:1 Yearbook of International Environmental Law 13; Iris Borowy, *Defining Sustainable Development for Our Common Future: A History of the World Commission on Environment and Development (Brundtland Commission)* (Routledge, 2014). See also Sumudu A Atapattu, Carmen G Gonzalez & Sara L Seck, eds, *The Cambridge Handbook of Environmental Justice and Sustainable Development* (Cambridge University Press, 2021).

on, or breed customary international law. In such cases, treaty law is seen as reinforcing or codifying existing customary rules rather than contradicting them. There is thus a general consistency nexus that pushes for treaties and customary international law to operate as complementary components that need to be harmonized through systemic interpretation where customary international law—notably, as it evolves—informs the interpretation of treaty provisions and thereby ensures coherence within the broader legal order.

However, even in situations of general consistency between a body of custom related to a treaty, conflict between given obligations in the treaty and in custom can occur. In particular, treaties can create *inter se* exceptions for or modifications to the existing rules of customary international law (excluding *jus cogens*) by deviating from certain obligations required by customary international law.[887] In such instances, under consent-based exception to custom, a smaller group of actors—any group smaller than the generality of States governed by the custom, but usually a much smaller group—carve out an exception from generally applicable norms of custom. The result is treaty law and customary law pointing in conflicting directions for dealing with those obligations (an actor being forced to violate one obligation in order to comply with another). Here we need a test of norm-by-norm actual conflict of obligations instead of examining consistency between two bodies of law—namely, there is a conflict if it is impossible for the obliged actor to meet one obligation without violating the other. We then turn to one branch of the principle of *lex specialis*—in the sense of a specific group of States consenting to set aside general norms—that requires that the reciprocal interests of the parties must be achieved by applying the special norm to which the sub-set of States have agreed. In such cases, *lex specialis* serves as a rule of priority, allowing the specific treaty norm to replace/override the general customary rule—but only as far as the conflict goes (and, it goes without saying, only in the relations amongst the members of the sub-set of States and not in the relations with those States and any other State that is not party to the treaty exception). Also, as discussed in Chapter 2, the fact that there is a conflict between two specific norms does not mean that the norm being "set aside" does not continue to exert an interpretive influence—for example, over the scope of the exception and with respect to other provisions in the treaty.[888]

[887] This has been discussed already in Chapter 2, so what follows is a recap.
[888] Koskenniemi, *supra* note 406.

As well, the body of law of which the excepted customary obligation is a part continues to apply—either directly as the most pertinent norm or interpretively in relation to a treaty in the other field—and is not affected by norm-by-norm exceptions. The example of ICJ's decision in the Legality of the Threat or Use of Nuclear Weapons case is very clarifying in this respect. In the case, the ICJ acknowledged that the right to life under human rights law still applied during war, but its interpretation—specifically what counts as "arbitrary deprivation of life"—had to be assessed according to humanitarian law, the *lex specialis* in that setting. This means that *lex specialis* narrows or adjusts the application of general law without eliminating it altogether. Even as it works so as to justify recourse to an exception, what is being set aside does not vanish altogether. The Court was careful to point out that human rights law continued to apply within armed conflict. The exception, humanitarian law, only affected one aspect of it, namely the relative assessment of "arbitrariness." The Court ultimately framed the two bodies of law—human rights law and the laws of war—as interconnected, representing both the ideal goals of peace and the realities of conflict, and balanced them pragmatically rather than applying one set in isolation. Accordingly, it could be concluded that in confrontation with the idea of exception (set aside, carve out), there is a difference between one body of norms derogating from another body of norms and one individual obligation excepting from another individual obligation (one each from a body of norms). Thus, it is clear that one obligation setting aside another obligation does not oust the ongoing interpretive relevance of the body of law to which the set-aside norm belongs as it would still inform interpretation of other non-conflicting treaty provisions.

To determine the relevance of customary law on corporate responsibility for sustainable development, consistency between any given rule of an investment treaty and the UNGC's environmental principles should be ascertained in order to justify having recourse to the UNGC as liability law.[889] We already know there is value compatibility—and a form of consistency in that general sense. And we already know that one way to characterize corporate responsibility law and investment law are as two fields tightly connected to sustainable development law as subject-matter—so we would have an expectation of harmony amongst norms from the same

[889] The question then is whether those provisions are exclusive, i.e. whether the consequences which would otherwise apply under general international law, or the rules that might otherwise have applied for determining a breach, are thereby excluded, *Ibid* at 50.

(which could be called another form of general consistency). But the consistency of which we speak here at this second stage of the "relevance" test is a norm-by-norm one and not a general one: if there is an actual conflict between a customary obligation and a treaty one (one cannot perform the customary obligation without breaching the treaty obligation). Here, only so much can be said because everything will depend on the textual expression of an obligation in a given investment treaty and the specific UNGC-related customary norm being invoked. What can be said, in advance of a particular comparison of an obligation associated with one or more of the UNGC's principles and an obligation in a given investment treaty, is that the UNGC's principles are worded generally enough that they do not, on their face, suggest the likelihood of a conflict unless a treaty norm has been carefully drafted to be a precise carve-out. For example, if a treaty had a provision specifying something like the precautionary principle for purposes of this convention shall be understood to mean, and to mean only, U, V, and W; and it was found that the precautionary principle as it has evolved within the UNGC regime (as itself influenced by general international law of environmental protection) also requires X, Y, and Z, then a tribunal would be faced with the need to apply the treaty as a *lex specialis* to determine the customary norm is inconsistent and thus not relevant if the issue at stake requires one party or the other to benefit from X, Y or Z.

Rare as such express narrow definitions of a customary principle may be, this example is not fanciful as it lines up with the phytosanitary arbitration discussed in Chapter 2.[890] In general, however, one can expect few similar examples—either because an investment treaty may have been drafted well before consciousness of sustainable development had fully infused thinking or because drafters of newer treaties have to take the conscious decision to depart from norms that they know they are generally expected to abide by (whether those norms are "soft law" in a sense understood as non-binding or whether norms are treated as transnationalized custom). The latter reason for such clear and direct conflicts being rare flows, in effect, from the kind of general consistency that is already apparent on the analysis of the "sameness" of the fields from a

[890] See Chapter 2 for the discussion on *United States: Import Prohibition of Certain Shrimp and Shrimp Products,* WT/DS58/AB/R, Report of the Appellate Body 12 October 1998, *supra* note 881.

purposive, contextual and category-characterization perspective. That is, we should not expect to find many actual conflicts.

To recap the sameness discussion, analyzing investment treaties and the UNGC's principles reveals that they are consistent in a way that the UNGC—as a transnationalized customary international law—has evolved overtime to provide clearer and more precise expression of sustainable development, than that of investment treaties, in particular, with regard to environmental obligations of foreign investors. As discussed above, preambular references to sustainable development and express protections for environmental considerations—not carve-outs from such protection—in contemporary investment treaties reflect how their provisions accommodate and reinforce environmental principles of the UNGC.

Thus, we find ourselves generally in the realm of the UNGC informing the meaning of treaty provisions, particularly in relation to investor environmental obligations, and principles of good governance. As customary sustainable development law expands and evolves, the UNGC becomes the source of a more detailed articulation of investors obligations that operate as complementary components of investment law.

We cannot discount that actual conflicts of obligations can arise. It is even conceivable that they might become less rare if certain new treaties consider more stringent carve-outs once the parties come to realize that tribunals are treating relevant sustainable development norms as customary law and are prepared to bear the criticism from stakeholders observing the negotiation of new treaties that contain such carve-outs. However, for the most part, we should not expect the consistency stage of the relevance analysis to often find actual conflicts. Rather, the relationship between investment treaties and the UNGC will be governed by a dynamic of harmonization through systemic interpretation where the UNGC—notably, as it evolves and shapes, and is shaped by, law influenced by the arrival of the SDGs—informs the interpretation of treaty provisions.[891]

[891] Koskenniemi, *supra* note 406.

In conclusion to the relevance discussion, one way to represent the expectation of harmonized interpretation versus the likelihood of inconsistent obligations is to set out a comparison of the aspect of a broad theme associated with investment treaties, on the one hand, and the UNGC, on the other—and to see the essential harmony between the aspects and see as well why one should not expect to see many actual conflicts:

1) **Tools for Sustainable Development**
   - Investment treaties do exist to protect investors. But—from the perspective of the States ageing to protect investment—their underlying rationale is that investment contributes to economic development and improved living standards—socio-environmental benchmarks—in host States.
   - The UNGC reinforces this goal by ensuring that businesses operate responsibly and contribute positively to host States' social, environmental, and economic progress.
2) **Legal Certainty and Responsible Investment**
   - Investment treaties provide a stable legal framework to encourage foreign investment, which in turn facilitates infrastructure development, job creation, and green technology transfer.
   - The UNGC ensures that investment is conducted in a way that does not undermine human rights, labor rights, or environmental sustainability, aligning economic interests with broader societal goals.
3) **Investor Obligations and Host State Responsibilities**
   - Investment treaties primarily focus on host States' obligations to provide a favorable investment climate.
   - The UNGC primarily emphasizes investor responsibilities in upholding sustainable development**.**
   - When applied together, with each set of obligations forming a whole, both frameworks are part of a broader legal framework to enhance sustainable development and create a consistent approach where there no actual conflict among their rules.

4.3.4 Applicability of the UNGC for Investment Treaty Interpretation

Under the traditional state-centric notion of international law, law is understood as the command of a sovereign, backed by enforceable sanctions, and norms lacking formal state consent or

binding obligations—such as the UNGC—are often dismissed as mere soft law.[892] This notion has historically reinforced the idea that only state-generated norms have legal normativity, relegating transnational regulatory frameworks that are not interstate and centered on treaties, like the UNGC, to the periphery of international law. However, this rigid state-centric understanding of law is increasingly challenged by socio-legal pluralist perspectives and transnational law approaches, which recognize the normative force of self-regulated norms arising from the interaction between States and non-state actors. As a scholar influenced by these perspectives, I seek to reassess the legal status of the UNGC beyond its conventional categorization as transnational self-regulated soft law. In this approach, there is no trust in an exclusive law-generating authority assigned by many to States. Instead, I argue that the UNGC, in specific circumstances, amounts to transnationalized customary international law, on equal footing with norms originating from conventionally recognized authoritative powers.

In the following discussion, I will question whether the UNGC could be treated as *applicable* law by ISDS tribunals in the treaty interpretation process. This requires me to examine both the *opposability* of the UNGC between the disputing parties and the legally *binding* nature of the UNGC on the disputing parties in order to be involved in resolving the substantive aspects of disputes. Examining the UNGC from its institutional dimension and its normative dimension is an integral step for me to claim that the UNGC, which is a self-regulated normative regime, could acquire the legal status of transnationalized customary international law, could be invoked by host States as liability law, and most importantly could be validated by investment arbitrators as applicable law in interpreting investment treaties. To do so, I draw on hybrid theory and interactional theory, to analyze legitimacy of the UNGC as a transnationalized customary international law. This analysis clarifies that the UNGC represents a new form of transnational legality—one that operates on equal footing with traditionally recognized sources of international law in specific legal contexts, particularly in investment governance and corporate accountability frameworks. As such, it feeds into the capacity of ISDS tribunals to strike a better balance between investors' interests and host States' values by holding foreign investors environmentally responsible for violating the UNGC's principles.

[892] Simon Roberts, "After Government? On Representing Law Without the State" (2005) 68 Modern Law Review 1.

4.3.4.1 Institutional Dimension

The UNGC is an example of a corporate governance institution that displays characteristics of emerging transnational self-regulated norms and thus raises questions regarding its functions and lawmaking powers. To address these questions, I analyze the UNGC from the transnational law perspective and offer new insights with regard to its lawmaking *actors* and the *function* played by its norms. From mere factual evidence, the UNGC poses challenges to the traditional state-centric approach to lawmaking, as it is developed through interactions between States and non-state actors such as transnational corporations. In addition, from the functional perspective, compared to other corporate governance codes, the UNGC does not directly emphasize market efficiency. Instead, it considers justice values as well. These two skews from the traditional lawmaking process—trusts in States as sole authoritative power and makes a firm demarcation between the public and private functions of law—raise serious issues regarding the applicability of the UNGC, as a rule of law, in ISDS tribunals.

Discussion of the hybrid theory in Chapter 3 suggests that the legal status of the UNGC, and consequently its applicability in the investment treaty interpretation, could be examined primarily according to its institutional dimension. Building on that hybrid theory discussion, I seek here to unfold the institutional dimension of the UNGC in order to draw out the complex correlations between diverse functions of the UNGC and various lawmaking powers engaged in its development process. This illuminates that States and non-state actors are cooperating to develop the UNGC with the goal of both maintaining justice in global society and enhancing the efficiency of the globalized market economy.

4.3.4.1.1 Hybrid Lawmaking Actors

The UNGC's hybrid nature stems from the various range of actors involved in its development and implementation, including States, international organizations, transnational corporations, and various non-state actors making up civil society. Kofi Annan's call at the 1999 World Economic Forum in Davos underscored this multi-stakeholder engagement by explicitly inviting business leaders to join the UN in promoting shared values and principles that would humanize the global market: "I propose that you, the business leaders gathered in Davos, and we, the United Nations, initiate a global compact of shared values and principles, which will give a human face to the

global market." This invitation marked a paradigm shift in global governance, acknowledging the private sector as an essential partner in achieving SDGs.[893] And the invitation was extended on behalf of an international organization that is more than simply the sum of the will of its states party members.[894] That is to say, two actors beyond States were invited to enter into a partnership. These participants—along with States and other participants who come to be involved, like non-governmental human rights and environmental organizations—contribute to the evolution of corporate responsibility in a globalized economy by shaping, implementing, and monitoring sustainability norms.

The UNGC, which embraces sustainable development while recognizing that significant improvements can only be attained through UN-fostered collaborative efforts among States and corporations, was developed as "a pragmatic response to government-governance failures."[895] From this viewpoint, the UNGC's greatest significance is to foster a new era of cooperation between the UN and the business community, especially transnational corporations, to address governance gaps at both national and international levels. It then operates as a framework that fosters dialogue and cooperation among these actors, allowing them to collectively advance the principles of human rights, labor rights, environmental sustainability, and anti-corruption. This approach recognizes that sustainable development cannot be achieved through state action alone but requires active corporate participation. This multi-stakeholder engagement ensures that the UNGC remains relevant and impactful, driving progress toward a more ethical and sustainable global economy.

Historically, the relationship between the UN and the business community has evolved significantly. When the UN was founded in 1945, it aligned closely with the ideology of the ICC, which viewed trade and investment as essential to political and social freedoms. The prevailing

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[893] Kell, *supra* note 843 at 69.
[894] The *Reparations* case, formally known as *Reparations for Injuries Suffered in the Service of the United Nations,* International Court of Justice (ICJ), Advisory Opinion 11 April 1949. It is a landmark case in international law because it clarified that the UN enjoys an international legal personality separate and apart from the States that agreed to form the UN by treaty and thus it has the legal power to bring international claims.
[895] *Reparations for Injuries Suffered in the Service of the United Nations,* International Court of Justice (ICJ), Advisory Opinion 11 April 1949.

belief was that fostering trade and investment would lead to greater economic interdependence, which, in turn, would contribute to global peace and prosperity. During this period, multinational corporations were generally viewed as agents of purely economic development, particularly in post-colonial and war-torn regions where foreign direct investment was seen as a means of fostering industrialization, infrastructure development, and employment opportunities. The business community, for the most part, was an active supporter of the UN's mission, particularly in the context of economic recovery and reconstruction efforts in the aftermath of World War II.[896] However, during the 1960s and 1970s, Cold War-era ideological shifts led to increased scrutiny of transnational corporations. Many newly independent nations, particularly in the Global South, viewed transnational corporations with skepticism, associating them with neo-colonial exploitation, environmental degradation, and economic inequalities. This perspective was reinforced by a series of corporate scandals, including human rights violations, environmental disasters, and unethical business practices, which fueled calls for greater regulation of multinational enterprises.[897] In this period, the UN responded to these concerns by intensifying its scrutiny of transnational corporations.

The establishment of the UN Center on Transnational Corporations (UNCTC) in 1974 was a significant development in this regard.[898] The UNCTC was created to monitor and regulate the activities of multinational enterprises, particularly in developing countries, where their operations were often accused of undermining national sovereignty and (what later became understood as) sustainable development. The establishment of these institutions contributed to an almost complete alienation of the business community to the extent that businesses adopted an antagonistic attitude towards the UN. As a result, the relationship between the UN and the private sector became increasingly adversarial. Many corporations perceived the UN's regulatory initiatives as hostile to business interests, leading to a period of disengagement and mutual distrust. Business leaders began to see the UN as an institution primarily concerned with

[896] Dominic Kelly, "The International Chamber of Commerce" (2005) 10:2 New Political Economy 259–271.
[897] Eva Nilsson & Martin Fougère, "Global South States' Views on Building Partnerships with Corporations: An Agonistic Struggle in the UN and Beyond" (2025) 197:3 Journal of Business Ethics 445–463.
[898] Sabine Ulrike Selchow, "The UN Economic and Social Council's Initiative on Multinational Corporations (1972-1974): A Primer" (2023) ECOINT Primer Series, European University Institute.

imposing constraints on corporate activities rather than facilitating economic cooperation and investment.[899]

This ideological conflict came to an end with the fall of the Berlin Wall in late 1989, when the UN General Assembly declined in support for binding international regulations on transnational corporations.[900] In 1992, the UN acknowledged that the changing international environment necessitated a cooperative approach for the relationship between member States and the business community. During this period, the UN started to reassess its relationship with the private sector, recognizing that achieving its development goals required active collaboration with businesses rather than confrontation. Instead of attempts at stringent regulations on transnational corporations, fostering voluntary cooperation that engaged businesses in corporate responsibility initiatives emerged as a preferred alternative. The turning point came with the election of Secretary-General Kofi Annan in December 1996, when the rapid growth of foreign direct investments underscored the globalized market economy's central role in tackling poverty while at the same time intensifying environmental issues. In order to find incentives that would attract the business community's attention towards the essence of sustainable development while convincing its member States that an institutional change and an effective UN/business relationship were needed for realizing the UN's SDGs, Kofi Annan organized several meetings with the International Chamber of Commerce, and joint statements were issued in 1998 and 1999 to introduce a new era of cooperation. This was cultivated in cooperative partnerships between the UN member States, who recognized the integral role of business in sustainable development, and the business community, who viewed the UN as an important participant in the globalization

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[899] Frederick I Nixson & Mchammed Yamin, "The United Nations on Transnational Corporations: A Summary and a Critique" (1980) 6:1 Review of International Studies 16–31.

[900] See Tagi Sagafi-Nejad & John H Dunning, *The UN and Transnational Corporations: From Code of Conduct to Global Compact* (Indiana University Press, 2008). This book provides a comprehensive analysis of the United Nations' evolving relationship with transnational corporations, detailing the ideological shifts and policy changes that occurred after the Cold War. It discusses how the UN moved from a confrontational stance, characterized by attempts to regulate transnational corporations through a binding Code of Conduct, to a more collaborative approach, exemplified by initiatives like the UNGC, that recognizes the importance of engaging the private sector in achieving SDGs.

debate. This period marked a transition in the UN's engagement with the private sector.[901] The focus shifted towards encouraging corporate social responsibility and partnerships between the UN and businesses to achieve development goals, exemplified by initiatives like the UNGC.

A logical extension of this approach favouring partnerships and constructive interactions was the UNGC, whose institutional network would come to emphasize how States and the business community can and must cooperate to promote economic efficiency and protect socio-environmental justice.[902] With an understanding that "state governance failures—the unwillingness or inability of governments to live up to their own commitments—are among the main reasons that the consequences of globalisation are so painful," it was widely recognized that sustainable development issues would be addressed through active participation of corporations in the governance process.[903] The UN noted that it would lack that capacity to achieve SDGs if States act alone or in a different framework from that of the business community.[904] States came to change their perceptions about the role of business in society and developed the UNGC with a proposition to "invite businesses to internalize UN values and take action in support of broader UN goals for greater market sustainability."[905] Once established, governments have come to perceive the UNGC "as a complementary approach that does not compete with regulatory intervention but does offer an additional way of mobilizing private sector activities in support of public policy goals."[906] In addition, the UN proceeded, in the years after the formation of the UNGC, to deepen the sustainable development agenda, culminating in the 2015 articulation of SDGS and of Agenda 2030. It connected up the two processes and sees the business community's involvement in the UNGC as a crucial endeavor to achieve SDGs.

The launch of the UNGC signified a deliberate effort to rebuild trust and foster a cooperative relationship between businesses and global governance institutions. Unlike the adversarial dynamics of the 1970s, the UNGC positioned businesses as partners in achieving sustainable

[901] Iñaki Heras-Saizarbitoria, Laida Urbieta & Olivier Boiral, "Organizations' engagement with sustainable development goals: From cherry-picking to SDG-washing?" (2022) 29:2 Corporate Social Responsibility and Environmental Management 316–328.
[902] Kell, *supra* note 843.
[903] Ruggie, *supra* note 846 at 40.
[904] Kell & Levin, *supra* note 856.
[905] Kell, "12 Years Later", *supra* note 857 at 33.
[906] *Ibid* at 39.

development, fostering a more cooperative and constructive relationship between the UN and the corporate world. By providing a voluntary framework for corporate responsibility, the UNGC bridges the gap between regulatory oversight and market-driven solutions, positioning corporations as key actors in the pursuit of global sustainability. Its hybrid nature, involving both States (including the interstate UN) and non-state actors, challenges traditional legal distinctions between public and private governance, highlighting the evolving role of transnational business entities in shaping international norms and advancing sustainable development.

The UNGC is a collaborative solution that has proven to be a "vibrant public-private initiative" to bring about positive change and develop functional dialogues involving multiple stakeholder groups.[907] In this context, the long-term vision of the UNGC to create an "inclusive and sustainable global economy" is deeply connected to the core vision of the UN regarding economic and societal development—including as that vision took shape through the development of the SDGs. The network-based institutional structure of the UNGC is also evident via the placement of the Global Compact Office as an entity within the UN to not only advance the role of the private sector through learning, dialogue, and partnerships but also to give "essential legitimacy and universality to the principles of the Compact."[908]

The engagement of these hybrid participants within the UNGC illustrates its role as a dynamic and inclusive platform for shaping corporate responsibility in the globalized economy. Unlike traditional regulatory frameworks that rely solely on state authorities, the UNGC thrives on collaboration among diverse actors, allowing businesses, governments, civil society, and international organizations to co-create sustainability norms. This multi-stakeholder approach ensures that the UNGC remains a flexible and adaptive mechanism for addressing pressing global challenges, from climate change and human rights abuses to corruption and social inequality. By integrating non-state actors into the global governance landscape, the UNGC challenges traditional distinctions between public and private authority. It redefines corporate responsibility by positioning businesses as essential partners in achieving sustainable development, rather than merely subjects of State regulation. This hybrid governance model of the UNGC embodies the

[907] *Ibid* at 32.
[908] Jon Burchell, "The United Nations Global Compact: Advancing Corporate Citizenship" in Jon Burchell, ed, *The Corporate Social Responsibility Reader* (Routledge, 2008).

dynamic nature of international norms. The UNGC norms—centring on the 10 principles while evolving beyond their pure textual expression in tandem with the evolution of SDG-centred sustainable development law—generates a body of transnationalized customary international law, exerting influence on corporate behavior toward environmental protection. The UNGC transcends traditional state-centric frameworks to establish sustainable development-related expectations and standards in transnational business practices, transforming them into transnational normative customs that may be understood as law.

It is important to recall that the ten principles of the UNGC do not function as static, standalone norms that by themselves constitute customary international law. Rather, these principles must be interpreted in light of the broader, evolving body of sustainable development law. While the UNGC principles serve as a foundational core, their normative influence has deepened and expanded through their interaction with subsequent developments such as the SDGs. Accordingly, the concept of transnationalized custom should not be understood as a simple textual reading of the UNGC principles akin to treaty interpretation. Instead, it reflects a dynamic and evolving process whereby these principles inform and are informed by an emergent, partly unwritten body of norms. To avoid a text-centric portrayal of custom, it is essential to emphasize that the UNGC principles evolve in both meaning and scope, shaped by ongoing legal, institutional, and normative developments in the field of sustainable development.

4.3.4.1.2 Hybrid Functions

To fully understand the hybrid functions of the UNGC, it is essential to examine, on one hand, the obligation of States to recognize transnational corporations as key actors in achieving the UN's SDGs. On the other hand, it is equally crucial to analyze how the globalized market economy must integrate socio-environmental justice and acknowledge legal frameworks that extend beyond the narrow focus on economic efficiency to ensure long-term sustainability. From this perspective, the UNGC positions itself as a stabilizing force that bridges the gap between economic imperatives and social responsibility. By promoting market inclusion and fostering responsible business practices, the UNGC tries to align (as) seamlessly (as possible) with the broader mission of sustainable development. Its role becomes even more critical in light of the persistent lack of decisive state leadership in addressing sustainability challenges, particularly concerning environmental protection within the investment sector. This hybrid structure enables

the UNGC to function as a transnational governance mechanism that not only guides economic efficiency but also reinforces the sustainability norms in the absence of binding international regulations.[909]

Thus, it is that the UNGC operates as a hybrid governance framework that integrates both public regulatory goals and private corporate advantages, fostering a cooperative model of global governance. This hybrid function stems from the recognition that neither governments nor corporations alone can fully address the complex socio-environmental challenges of a globalized economy.[910] The environmental principles of the UNGC, as their meaning evolves in light of the influence of the SDGs, serve as a guiding framework for companies, encouraging them to adopt responsible business practices. By aligning their strategies and operations with SDG-informed UNGCs, companies contribute to a level playing field in terms of environmental responsibility—thus ensuring fairness of competition—while simultaneously advancing substantive justice goals of environmental and kindred protections. This approach is increasingly gaining recognition and is becoming a crucial aspect of responsible business practices.[911]

It can be seen that, instead of bringing direct economic benefits to signatory corporations of the UNGC, the principles of the UNGC point to private corporations and emphasize their duties towards environmental justice. Hence, one of the key concerns regarding corporate adherence to sustainability principles, such as those in the UNGC, is whether they impose additional financial burdens without immediate efficiency (translating into profit) gains—and, if so, whether that is simply the kind of trade-off that is required if business and environment are to find an equilibrium point. The latter must surely be the case—especially if one adds the premise that, along with promoting the public values of environmental justice, corporations joining the UNGC will also benefit from the positive effect of the UNGC on their long-term portfolio performance by suffering lower volatility and carrying less risk than their competitors.[912] *The UN Global*

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[909] McIntosh, Waddock, & Kell, *supra* note 827.
[910] Kell, "12 Years Later", *supra* note 861.
[911] "UN Global Compact & BPW", online: *BPW International* <http://www.bpw-international.org/partnership/un-global-compact/>.
[912] Moses Msiska, Alex Ng & Randall K Kimmel, "Doing well by Doing Good with the Performance of United Nations Global Compact Climate Change Champions" (2021) 8:321 Humanities and Social Sciences Communication at 1.

Compact 2022 Annual Report illustrates that "90% of surveyed companies confirmed that the UN Global Compact has helped them advance corporate responsibility policies and practices" [913] to improve their reputation,[914] to expand their transnational commercial interactions,[915] and to enhance their economic efficiency.[916] Empirical studies suggest that firms integrating sustainability-oriented business models tend to experience long-term economic benefits, including:

- **Lower Investment Risks and Volatility:**
  Companies that align with the UNGC principles tend to attract long-term investors, as they demonstrate resilience against financial shocks and regulatory risks. UNGC-compliant firms have been shown to suffer from lower market volatility and reduced risk exposure, leading to more stable financial performance.
- **Enhanced Corporate Reputation and Consumer Trust:**
  Consumers and stakeholders increasingly demand ethical and environmentally responsible business practices. Firms adhering to UNGC principles benefit from stronger brand loyalty, competitive differentiation, and increased market share.
- **Access to Sustainable Finance and Investment Opportunities:**
  Investors who are increasingly integrating sustainable development requirements into their decision-making are more likely to receive preferential treatment in capital markets. UNGC compliance boosts a company's credibility and appeal to investors focused on responsible and sustainable finance.

[913] United Nations Global Compact (UNGC), *supra* note 823 at 7.
[914] Jorge A Arevalo & Deepa Aravind, "Strategic Outcomes in Voluntary CSR: Reporting Economic and Reputational Benefits in Principles-Based Initiatives" (2017) 144:1 Journal of Business Ethics 201–217; Kjetil Selvik, "Business and Social Responsibility in the Arab World: The Zakat vs. CSR models in Syria and Dubai" (2013) 12:1 Comparative sociology 95–123.
[915] Daniel Berliner & Aseem Prakash, "From norms to programs: The United Nations Global Compact and Global Governance" (2012) 6:2 Regulation & Governance 149–166.
[916] For a comprehensive discussion on how UNGC can enhance financial performance of member corporations, see Msiska, Ng & Kimmel, *supra* note 912. For the scientific and empirical debate on the positive impact of UNGC on firm performance, see Guido Orzes et al, "The impact of the United Nations global compact on firm performance: A longitudinal analysis" (2020) 227 International Journal of Production Economics. Citra Hennida, "Compliance on the UN Global Compact" (2017) 1 Proceedings of the 2nd International Conference on Sociology Education 184–189 explains how UNGC enhances a reputation for signatory companies.

Therefore, the UN partnership with corporations through the UNGC is established based on the ideology that free trade and open markets will be enhanced through more socially responsible behavior and that seeks to align the socio-environmental responsibilities of corporations with their economic interests to maximize the benefit of the globalized economy. As noted by Post, "businesses cannot expect to reap the benefits of open global markets without acknowledging—and responding to—their social and political responsibilities."[917] Businesses learn that markets must be embedded in broader frameworks of justice values and shared objectives to survive and thrive. Some companies have done environmentally risky performances in the past; they have paid a price of public embarrassment and perhaps even diminished sales or stock values, and they now want to pursue a different path. Others want to make sure they do not repeat the errors their peers have committed.

The UNGC, in this respect, is a vehicle that offers one viable and vital approach to meet justice values at the same time as the efficiency dictates of the market economy. Thus, the UNGC's environmental principles are regularly defined as the backbone of fair competition and overall social and economic welfare, taking place in the context of far-reaching concerns regarding economic competitiveness and adaptability to the volatile demands of global capital. Therefore, the institutional aspect of the UNGC' principles provides the UN member States with an advantage in dealing with the burgeoning debate around SDGs and also offers signatory corporations the ability to sustain their financial success over time.

Against this background, transnational self-regulated norms—instead of being dismissed as contrary to the dogma of the State as the exclusive author of law—are developed out of constant interactions between hybrid lawmaking actors while playing the conjoined functions of promoting justice and enhancing efficiency in the globalized market economy. These norms show the complex interplay between official and unofficial norm-making processes that not only refute the contention that States must be understood as the sole author of law but also show the distinct regulatory quality of norms produced by a growing number of non-state lawmaking powers. The UNGC is a network of autonomous actors, each with different interests and needs that intersect

[917] James Post, *Meeting the Challenge of Global Corporate Citizenship* (Boston, MA: Boston College Center for Corporate Citizenship, 2000) at 2.

only partially, who cooperate in perceiving, understanding, and framing aspects of their behavior through collective principles. These norm-making processes we have identified above are fuzzy (even messy) in the sense that the identification of either co-ordinative or regulatory functions no longer occur based on distinguishing between the public or private nature of the actors involved. Instead, the environmental principles of the UNGC were identified on pragmatic grounds—versus a doctrinaire division of norms into public and private realms—in order to be responsive to critical legal issues surrounding the role of corporations in an era of global economic integration and to the core institutional competence of the UN to play the role of integrating justice concerns with efficiency values in the globalized economy.

However, the legal status of the UNGC cannot be determined solely based on its hybrid institutional nature. Rather, it also hinges on the normativity and legitimacy of its principles, particularly in relation to their influence on corporate behavior. A critical issue arises: to what extent do the UNGC's environmental principles create legal obligations for corporations to adopt environmentally responsible practices? From its inception, it was evident that the UNGC, as a network-based voluntary initiative, could not derive legitimacy from centralized state decision-making. Unlike traditional command-and-control governance models, where state authority enforces compliance through legally binding regulations, the UNGC operates through voluntary commitments rather than coercive top-down regulation. This demand-driven approach raises concerns about whether the UNGC's principles can be considered legitimate and normative, especially given that they do not expressly purport to impose direct legal obligations on corporations. To address these concerns, the next section applies interactional theory to assess the UNGC's normativity. This approach examines how the legitimacy of the UNGC arises from the interactive process through which its principles are formulated, internalized, and implemented by corporate actors. By evaluating the institutionalization of these norms in corporate governance frameworks, I aim to clarify how the UNGC, despite its threshold voluntary nature, can exert legal influence and function as a transnational normative framework shaping corporate environmental responsibilities as a matter of transnationalized customary international law.

4.3.4.2 Normative Dimension

Legitimacy is a crucial aspect of determining whether the UNGC norms might be treated as *applicable* liability law in ISDS tribunals. In the traditional lawmaking framework, legal norms would obtain legitimacy through state consent, either when they are directly created by recognized forms of state (or interstate) power or when they are incorporated by reference by state power—taking on the quality of state or interstate law, albeit as a category with subordinated status in confirmation of state-law supremacy.[918]

However, with respect to the hybrid institution of the UNGC, the transnational legal perspective argues that the legitimacy of the UNGC should be recognized by those who both create the norms and are subject to the norms.[919] This means that although the UNGC has not gone through the state/interstate consent procedures to become a rule of international law, it is not necessarily equivalent to the UNGC being non-binding.[920] With this in mind and recalling the Chapter 3 discussion, I apply interactional theory to explain how a sense of juridical obligation, which is the added value that distinguishes law from other forms of normativity, towards the UNGC's principles is created among signatory companies and UN member States through the interactional dynamics of the UNGC.[921]

Whether or not the UNGC is applicable in the investment treaty interpretation process is not answerable with regard to its enforcement mechanism. Instead of focusing solely on form—formal bindingness and institutional enforcement—interactional theory claims that the distinctiveness of legal norms organically emerging from social norms lies in the realm of substance and sociology—namely, the creation of a sense of legal obligation that complements what is otherwise merely social (or, put another way, that produces only a socio-ethical, but not a juridical, sense) around those norms. Indeed, through the lens of the interactional theory, compliance mechanisms and enforcement measures are not outcomes produced by or imposed on

[918] Berman, *supra* note 631.
[919] Cotterrell, *supra* note 586 at 263.
[920] Matteo Podrecca, Marco Sartor & Guido Nassimbeni, "United Nations Global Compact: Where Are We Going?" (2021) 18:5 Social Responsibility Journal 984–1003.
[921] See

legal norms but are part of the continuing process of making legitimate law. In the context of the UNGC, this process should be assessed in accordance with 1) interactional roots of shared understandings, 2) adherence to specific criteria of legality, and 3) continuous practices of legality.

As discussed in Chapter 3, the interactional theory, when integrated with a Fullerian idea of legality and its indicators, can demonstrate the normative nature and legitimacy aspect of the contemporary practice of transnational lawmaking and illuminate why and how legal obligations at the transnational level can result from such interactions. Instead of focusing solely on form—voluntary entry into a process, compliance mechanisms that are not typical for traditional state law, or the formal description of instruments in which the norms are embedded—interactional theory claims that the distinctiveness of legal norms from social norms lies in the realm of substance and sociology—namely, the creation of a sense of obligation beyond the merely social (or, put another way, socio-ethical) around those norms. In light of the interactional perspective of transnational self-regulated norms, the UNGC, despite its non-binding nature and differing from other international corporate governance frameworks such as the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct,[922] could create a sense of obligation among transnational corporations to act in an environmentally responsible manner—where that obligation arises from more than self-given volition but rather from a sense of commitment generated by mutual relations with other participants in the network of interactions.

The interactional process of the UNGC confirms the fact that its objective is more than just proposing a set of non-binding codes of conduct with which corporations voluntarily comply. Instead of regulating how corporations should act in particular ways, the UNGC creates an environment in which corporations can—and come to—learn to collectively identify with environmentally responsible culture and comply with the pertinent associated obligations. This sense of obligation will be generated if:

[922] The OECD Guidelines for Multinational Enterprises on Responsible Business Conduct are recommendations offered by governments to multinational enterprises to encourage positive contributions enterprises can make to economic, environmental, and social progress, Organisation for Economic Co-Operation and Development (OECD), *OECD Guidelines for Multinational Enterprises on Responsible Business Conduct* (2023), online: <ttps://doi.org/10.1787/81f92357-en>.

1. the UNGC is or is essential to the interactional root of shared understandings (a legal norm requires the creation of legitimacy through the emergence of shared understandings between participants);
2. the UNGC adheres to specific criteria of legality (a legal norm will be further endorsed through meeting eight criteria of legality, as discussed in Chapter 3); and
3. the UNGC is the root or focal point for more than momentary adherence to specific criteria but rather for a continuing practice of legality (a legal norm must be maintained interactionally, that is, through a reciprocal practice of legality).

4.3.4.2.1 Interactional Roots of Shared Understandings

The UNGC has sought to develop from the beginning as an initiative with a variety of participants. It brings transnational and other kinds of corporations together with UN agencies, labor, civil society organizations, and governments in an effort to advance universal environmental and social principles in order to foster a more sustainable and inclusive world economy.[923] With this objective in mind, the UNGC is built based on shared understanding among diverse actors. The setting for shared understanding is an interactional learning process that is furnished by a community of practice whereby corporations, society, and governments "are informally as well as contextually bound by a shared interest in learning and applying a common practice."[924] Through this community of practice, participants instantiate and sustain their shared understanding of benefits of globalization as well as of the backlash globalization's harms generate, as well as the appreciation of what it means to be an environmentally responsible corporation. Based on such shared understandings, the UNGC was developed and then maintained by the interactional networks focused on respecting and nourishing its principles.

Through these interactional networks, actors generate a collective understanding that the backlash against globalization has grown in direct proportion to the divergence between the globalized market economy and both the harms to and the under-benefiting of national communities.[925] Over time, they recognize that the backlash is triggered mostly by the unequal distribution of

[923] Burchell, *supra* note 913.
[924] Adler, *supra* note 738 at 15.
[925] For comprehensive discussion on the effects of increasingly integrated global economy on the environment and society, see Khi V Thai, Dianne Rahm & Jerrell D Coggburn, *Handbook of Globalization and the Environment* (Routledge, 2007).

globalization's economic benefits both within and among countries, by an imbalance in rules that promote global market expansion versus rules intended to promote equally valid social objectives, and by puzzlement about (rising to resentment of) authoritative powers (dis)organizing the global economy.[926] This leads to the conclusion that "the present state of affairs is not sustainable" and the gap between the market and national communities will not be closed unless corporations can align themselves with broader social and environmental goals or at least make sure that their actions do not undermine them.[927] That is where a shared understanding is developed about the socio-environmental responsibility of corporations that can address the burden of globalization by embracing universal values and concerns in the corporate sphere and weaving them into global market relations.[928]

The collective understanding of a culture of stronger environmental stewardship by corporations to manage globalization's challenges and sustain the global economy has led to the development of the particular norms and procedures of the UNGC.[929] These norms serve as reference points in the ongoing negotiation of global corporate socio-environmental responsibility, shaping how businesses integrate sustainability into their operations. As an inter-organizational network, the UNGC is not just a framework for corporate responsibility but a "global amalgamation of strategic and wide public policy learning networks that cultivates integrative learning."[930] It functions as a bridge between two seemingly contrasting paradigms—business as a profit-maximizing entity and business as an integral part of society that must generate value beyond economic gains while ensuring that its activities do not harm the environment.

Through this multi-stakeholder engagement, the UNGC has successfully developed a broad normative consensus on global values that promote corporate sustainability. It provides a platform to "promote responsible corporate citizenship, ensuring that business, in partnership with other societal actors, plays its essential part in achieving the United Nations' vision of a

[926] Kell & Levin, *supra* note 856.
[927] Annan, *supra* note 826.
[928] Ruggie, *supra* note 846.
[929] Brunnée & Toope, *supra* note 921 at 62.
[930] Kell & Levin, *supra* note 24 at 47.

more sustainable and equitable global economy."[931] This means that the UNGC does not merely suggest voluntary commitments but also influences corporate behavior by embedding sustainability into global business practices. Furthermore, this interactional process of norm development underscores how the UNGC is emerging as a legal regime in response to the widely recognized issues of global market failures, environmental degradation, and social inequities. By fostering a common understanding of global challenges, emphasizing the urgency of collective action, and defining the responsibilities of diverse actors, including corporations, States, and civil society, the UNGC solidifies its role as a transnational governance framework. In doing so, it ensures that corporate conduct aligns with long-term sustainability objectives, reinforcing the idea that economic prosperity and environmental integrity are not mutually exclusive but rather interdependent pillars of a stable global economy.

Crucially, reliance on shared understandings is not limited to the initial stage of developing the UNGC. This observation is crucial for understanding how the UNGC is the root of an ongoing, interactionally sustained practice of legality. Long after the UNGC's principles were enunciated and long after any given corporate actor signs on to them and the processes such adherence triggers, participants continue to collectively retain, deepen, and extend their shared understandings by bringing together the multiple perspectives and interpretations of global issues. According to *the UN Global Compact 2023 Annual Report*, the UNGC offers opportunities for learning and dialogue by engaging participants primarily through three mechanisms: dialogue events, learning events, and partnership projects.[932]

On the global level, the UNGC Leaders Summit annually brings together business, government, and civil society leaders for solutions-based discussions on how businesses can balance ethical and sustainable practices by complying with the UNGC's principles to maintain profitability and

[931] John Howard, US - EU Cooperation on Workplace Safety and Health (2005), online: <https://www.useuosh.org/conference2005/speech_2005>.
[932] United Nations Global Compact (UNGC), *UN Global Compact 2023 Annual Report* (2024), online: <https://ungc-communications-assets.s3.amazonaws.com/docs/about_the_gc/UN%20GLOBAL%20COMPACT%202023%20ANNUAL%20REPORT.pdf>.

competitiveness.[933] This annual Leaders Summit brought together almost 1,000 global leaders in corporate sustainability from 73 countries in-person in 2023. Programming centred on building awareness of the newly launched Forward Faster initiatives. Attendees were provided with global examples of how the private sector is increasing action in areas of Climate, Living Wage, Water Resilience, Gender Equality and Sustainable Finance. The Annual Country Network Forum, hosted in New York, fostered connection and collaboration among Global Compact Networks and with Headquarter staff. Throughout the year, Global Compact Networks also collaborated with headquarters teams in functional working groups, during in-person events, and in organization wide virtual town halls. On the sidelines of COP28 in 2023, the UNGC convened business leaders in Dubai, UAE to develop a Middle East spotlight guidance report on advancing male allyship for gender equality in the workplace. The UN Global Compact hosted a private-sector dialogue on due diligence and corporate action with vulnerable stakeholder groups. COP28 remained an important flagship event that included 54 meetings during which it welcomed almost 1,000 attendees, including high-level meetings of Caring for Climate, Africa Business Leaders Coalition, the Private Sector Reception, and a SDG Investment Forum.

These mechanisms of interactional engagement are extended to the regional level to facilitate exchange between the UNGC participants and to advance and support the UNGC's principles within countries around the world. The UNGC's local engagements are aimed at "moving innovative solutions upstream for global replication and multiplication, or … taking global dialogue issues down to the level of implementation" to create an engagement platform for promoting and displaying partnership projects.[934] On this issue, *the 2023 UN Global Compact Annual Report* offers detailed information on how the UNGC provided opportunities to engage

[933] "UN Global Compact Leaders Summit 2010 – Building a New Era of Sustainability", online: *United Nations* <https://www.un.org/en/desa/un-global-compact-leaders-summit-2010-%E2%80%93-building-new-era-sustainability>.
[934] Georg Kell, "The Global Compact Origins, Operations, Progress, Challenges" (2003) 11 The Journal of Corporate Citizenship 35–49 at 40.

participants and stakeholders—via think labs,[935] academy,[936] strategic convenings,[937] accelerators,[938] peer learning groups,[939] and policy advocacy and learning campaigns[940]—to accelerate responsible business practices and commitments on a broad scale for implementing UNGC's principles.[941]

Specifically, for bolstering shared organizational culture, regional coordination on governance, operations, and programming has strengthened in 2023, with the Regional Hubs now fully launched in Abuja, Bangkok, Copenhagen, Dubai, and Panama. In 2023, the UN Global Compact's Regional Meetings were hosted in the regions by Global Compact Networks in China, Colombia, Egypt, Georgia and Jordan to gather corporate sustainability leaders in the region. The UNGC also introduced the Africa platforms—the Global Africa Business Initiative and Africa Business Leaders Coalition—to promote sustainable investment and collaboration. The Africa Business Leaders Coalition sought to strategically enhance its brand and visibility by participating in events within the continent and on the global platform. In June, a gathering on the sidelines of the Africa CEO Forum assessed advancements in the Africa Business Leaders Coalition's Climate Statement and set the stage for the latter part of the year. During the inaugural Africa Climate Summit in September, the Africa Business Leaders Coalition conducted a plenary event and a private meeting, where participants formulated policy recommendations. In Beijing, China, the UN Global Compact unveiled guidance for Chinese companies to advance sustainable infrastructure under the Belt and Road Initiative. A private-sector dialogue was

[935] UN Global Compact's Think Labs convene representatives of businesses, academia, civil society, Government and the United Nations to develop solutions to critical corporate sustainability challenges. They help participants define their thinking, curate best practices, and develop the innovative knowledge, guidance and tools needed to inform business action on urgent topics.
[936] The Academy serves as the digital learning platform of the UN Global Compact, providing business leaders and practitioners with actionable skills for their sustainability journey. In 2023, the Academy experienced significant growth worldwide across key topics and innovative, new learning formats.
[937] The UN Global Compact convenes, inspires, educates, connects, and, most importantly, mobilizes global stakeholders to take bold action on corporate sustainability and the SDGs. Flagship UN Global Compact events include the annual Private Sector Forum, the Leaders Summit, and the Global Africa Business Initiative in addition to a wide range of regional and local events convened by Global Compact Country Networks.
[938] Accelerators, delivered in close collaboration with Global Compact Country Networks, are designed to generate behaviour change across companies at the country level.
[939] Meetings of UN Global Compact Peer Learning Groups create opportunities for groups of companies to share best practices and challenges at regional and local levels.
[940] Policy advocacy activities and timebound Call-to-Action campaigns are implemented to support policy positions and drive ambitious action at global and local levels.
[941] United Nations Global Compact, *supra* note 5.

hosted in Chile on due diligence and corporate action with vulnerable stakeholder groups ahead of a regional business and human rights forum. Also, a regional convening took place in Tbilisi, Georgia that gathered corporate sustainability leaders specifically from the European region.

Through these events, the mutual reinforcement of agents and structures within the UNGC is sustained through dynamic and influential interactions among participants. These interactions are driven by a shared understanding that continually evolves around the UNGC's core principles, ensuring that the initiative remains responsive to emerging global challenges. The UNGC serves as a platform for structured dialogue, enabling participants to collectively refine and broaden consensus-based definitions of best practices for achieving sustainable development. On the one hand, participants in the UNGC actively generate, promote, and refine particular understandings of corporate responsibility, shaping norms that emerge, evolve, or even fade away through social learning processes. This ongoing exchange of knowledge and experience fosters innovation in corporate sustainability practices while reinforcing the expectations placed on businesses to align with socio-environmental objectives. On the other hand, once these shared understandings become institutionalized, they influence how actors perceive themselves and the global landscape, define their interests, set priorities, and engage in discourse—and how they continue to engage to arrive at, deepen, and extend shared understandings of normative expectations. These norms guide decision-making, shaping the way businesses justify their actions and evaluate the commitments and arguments of others within the framework of global corporate governance. The central insight is that social interaction is the engine that drives these processes to "[o]pen up, maintain, and preserve the integrity of the channels through which diverse participants can communicate across the boundaries and through the barriers that ... separate" them.[942]

The continuous, network-based structure of the UNGC is precisely what has allowed it to rapidly become a critical reference point in the more general global debates and conversations on corporate sustainability and governance. By fostering sustained engagement that doubles as participatory governance, the UNGC effectively facilitates cross-sectoral collaboration, allowing for more adaptive and integrated approaches to complex global challenges. Without this

[942] Fuller, *supra* note 687 at 186.

interactional mechanism, the UNGC—as have and as do national governments, private firms, and social organizations acting independently or in isolation—would struggle to respond to the rapidly evolving and multidimensional issues that sustainable development efforts seek to address. Thus, the UNGC's legitimacy and influence stem from its ability to integrate diverse perspectives into an evolving framework of corporate responsibility, ensuring that businesses remain active contributors to global sustainability goals rather than passive observers or mere profit-driven entities.[943]

4.3.4.2.2 Adherence to Specific Criteria of Legality

The second essential requirement for fostering a sense of obligation among participants toward the UNGC's principles lies in the fulfillment of eight criteria of legality. Having established that the overall objective of the UNGC is rooted in shared understandings developed through a continuous interactional process, I now turn to an assessment of the extent to which its principles align with the criteria of legality—a crucial benchmark for determining the normative legitimacy of interactional law. Recall the presentation in Chapter 3 as to the origin of these criteria—sourced in the work of Brunnée and Toope who rely on and adapt the work of Fuller.

A corporation's ability to rely on the UNGC in its decision-making and to maintain a commitment to its principles is significantly strengthened when the UNGC adheres to fundamental requirements of legality. These criteria serve not merely as a checklist for assessing whether the UNGC can be classified as a rule of law, but rather as an integrated framework that actively reinforces corporate engagement with the UNGC's principles. By meeting these criteria, the UNGC plays an instrumental role in shaping corporate reasoning and behavior, fostering an ongoing process of mutual engagement, and deepening internationally shared legal understandings. Furthermore, adherence to these principles of legality contributes to the formation of a community of legal practice, where corporations, policymakers, and other

[943] The UNGC has been also criticized for failing to compel its signatory companies to meaningfully enhance their corporate social responsibility efforts or fully integrate its ten principles into their operations, leading to a significant loss of public trust. Moreover, its increasing dependence on corporate support has compromised its credibility and ability to effectively fulfill its mission, raising doubts about its long-term viability and usefulness. *See* Oliver F Williams, "The United Nations Global Compact: What Did It Promise?" in Gabriel Flynn, ed, *Leadership and Business Ethics* (Springer, 2022); and, already a decade ago, S Prakash Sethi & Donald H Schepers, "United Nations Global Compact: The Promise–Performance Gap" (2014) 122 Journal of Business Ethics 193–208.

stakeholders collectively refine and internalize corporate responsibility norms. This interactive and iterative engagement process nurtures a sense of fidelity to the UNGC's norms, reinforcing its practical legitimacy and influence in transnational governance.

Since the inception of the UNGC, its participatory framework has been designed to be universal and inclusive, ensuring that corporations across industries and regions—regardless of their size, financial standing, or market influence—can engage with its sustainable development agenda. This universality aligns with the legality requirement of ***generality***, a fundamental principle that ensures all member corporations are not only subject to the obligations of the UNGC but also entitled to partake in its decision-making processes. Given that corporations operate within and shape the global market, while also being directly impacted by its economic, social, and environmental challenges, the generality of the UNGC's principles becomes crucial in fostering a collective responsibility for sustainable business practices. This principle of inclusivity extends beyond major financial institutions or multinational corporations; it equally applies to small and medium-sized enterprises, reinforcing that every corporate actor holds both the capacity and the duty to contribute to global sustainability efforts.

The environmental principles of the UNGC particularly exemplify this broad applicability, as they articulate three overarching obligations for all signatory corporations:

- "Support a precautionary approach to environmental challenges," ensuring that businesses anticipate and mitigate environmental risks before they cause harm.
- "Undertake initiatives to promote greater environmental responsibility," embedding sustainability into corporate strategies and operations.
- "Encourage the development and diffusion of environmentally friendly technologies," fostering innovation that supports long-term ecological and economic resilience and, in relation to "diffusion," especially ensuring that environmentally-protective technologies that are used by a company in one jurisdiction are not treated as dispensable and, so, not used in another.

By framing these three environmental commitments in general yet, once concretized with examples, actionable terms, the UNGC establishes a baseline of corporate conduct that not only

drives global environmental governance forward but also creates a shared ethical and operational foundation for businesses to align with international sustainability standards. This generality ensures that corporate participation in the UNGC is not merely symbolic but actively contributes to shaping a more equitable, responsible, and sustainable global economy.

The UNGC fully satisfies the requirement of ***promulgation***, ensuring that its principles are transparently communicated, widely disseminated, and easily accessible to all stakeholders. Promulgation is a crucial legal criterion that guarantees norms are not only formally established but also effectively communicated to those expected to follow them. In the case of the UNGC, its principles are publicly available through its official website, annual reports, corporate sustainability disclosures, and various outreach programs, allowing corporations, policymakers, investors, civil society organizations, and the general public to engage with and understand its framework. Beyond mere accessibility, the UNGC actively promotes its principles through a multifaceted dissemination strategy. This includes:

- Global and regional conferences, such as the UNGC Leaders Summit, where businesses and stakeholders discuss best practices and implementation strategies.
- Training programs, webinars, and workshops, which provide corporations with guidance on integrating the principles into their operational frameworks.
- Sustainability reports and progress updates, in which signatory corporations are required to disclose their adherence to the UNGC's principles, fostering transparency and accountability.
- Collaborative initiatives with governments, non-governmental organizations (NGOs), and academic institutions, helping to expand awareness and drive adoption of responsible business practices across industries and regions.

By ensuring widespread and continuous promulgation, the UNGC not only makes its principles readily available but also actively fosters a culture of corporate responsibility, reinforcing its role as a guiding framework for ethical and sustainable business practices worldwide.
Nothing in the UNGC's environmental protection principles goes against the requirement of ***prospectivity***, identifying how individuals ought to behave in the future after the crystallization of a rule as law rather than prohibiting behavior that occurred before the rule became law. As with

any area of customary law, the law only applies to conduct that occurs after the norm has crystallized into law—unless there is a clear additional component of the rule that applies it, exceptionally, to conduct occurring previous to the rule becoming law.[944] As a matter of general international law doctrinal theory, the UNGC must be treated as prospective because to apply it retroactively violates the rule of law notion that one must know that one's conduct is illegal at the time of the conduct.

As an important aside, there is a different sense of prospectivity than the legality version just discussed. The need to apply the UNGC custom only prospectivity is all the more apparent when we note that the UNGC adopts generally forward-looking orientation required for addressing global environmental challenges. Here, the focus has not been whether norms that are later called laws apply to conduct before they become laws, but rather about emphasizing prospective change in behaviour over condemnation of past conduct as the dominant mode before the norms do become law. The UNGC's pre-legal emphasis on prospectivity not only has allowed companies time to develop awareness and understanding of what constitutes responsible conduct but also encourages companies to adopt and implement these principles moving forward, without retroactively holding them accountable for past actions before such norms have actually evolved into law that will, from that point forward, can apply to past conduct as liability law and not only to encouraging changed future conduct.

Overall, the UNGC effectively meets the requirement of ***clarity*** in its environmental principles, ensuring that member corporations can clearly understand their obligations. The environmental principles of the UNGC are clear in the basic expectations arising from the way they are phrased, making it possible for signatories to identify at least the core of their expected responsibilities

[944] See *Tanny c Procureur général des États-Unis,* Court of Appeal of Quebec (Montréal), Case No 500-09-030217-2282023, Judgment 2 October 2023, a Canadian case that treats custom as only applying as a matter of international law after a specific date of formation. In this case, the Quebec Court of Appeal addressed the application of retroactive legal provisions. The case involved a class action where the plaintiffs challenged the retroactive application of a provision under the State Immunity Act. The Court emphasized that declaratory provisions, by their nature, are intended to apply retroactively, affecting ongoing proceedings as if they had always been part of the legislation. This means that such provisions can alter the legal framework applicable to past conduct, provided that the legislature clearly expresses this intent. The Court's analysis underscores the principle that while retroactive laws can impact existing rights and obligations, their application must be grounded in explicit legislative language to ensure fairness and legal certainty.

and align their corporate strategies accordingly. One cannot overstate this, however, as they are still fairly generally worded (for example, there being no textual definition of precaution). But the rule-of-law, or legality, requirement for clarity is not a requirement for unworkable precision or detail.[945] Jurisprudence in jurisdictions the world over accepts that law must often be framed at a certain level of generality of expression and then be left to reasonable interpretation and concretizations by various law-applying actors. In that sense, clarity is about *sufficient* clarity where sufficiency connote the idea that the meaning given to the obligation cannot be so unknowable as to amount to arbitrary meaning. The meaning of generally worded norms requires processes of clarification—notably through authoritative application and interpretation—and not simply textual clarity from the outset.

Achieving clarity in environmental standards is inherently challenging because sustainability issues constantly evolve with new scientific discoveries and vary across different legal systems, making universally accepted definitions difficult. However, the complexity goes beyond just scientific and regulatory diversity—environmental standards are also politically contested, with various stakeholders holding conflicting interests. Some actors actively seek to weaken or undermine these norms to protect economic or political agendas, while others work to strengthen and expand them, resulting in multiple, often competing definitions and interpretations. Despite these complexities, the clarity of the UNGC's environmental principles is reinforced through its structured implementation processes that make clear what conduct corporations are striving to achieve and what conduct other actors are criticizing as inadequate. Corporations involved in the UNGC know that clarity is not solely derived from the text of the principles themselves but is continuously refined through participation in the UNGC's community of practice. Signatory

[945] Since its adoption in the 1992 Rio Declaration, the precautionary principle has become a central element of sustainable development, providing a legal framework to address serious or irreversible environmental and health risks despite scientific uncertainty. While it offers significant benefits—such as promoting preventive action, shifting the burden of proof to potentially harmful actors, and encouraging inclusive decision-making—the principle faces challenges including vague definitions that undermine legal certainty, inconsistent application, concerns about stifling innovation, and resistance from business and scientific communities favoring traditional risk assessments. These difficulties, combined with conflicts between precaution and economic interests, complicate the principle's consistent implementation, but it remains a vital tool for protecting the environment and public health in uncertain contexts. See *The Precautionary Principle: Decision-Making Under Uncertainty*, by European Union, in *Science for Environment Policy* (European Union, 2017) online: <https://blogs.uni-bremen.de/starbiosbremenenglish/files/2019/09/precautionary_principle_decision_making_under_uncertainty_FB18_en.pdf>; Carolyn Raffensperger & Joel A Tickner, eds, Protecting Public Health and the Environment: Implementing the Precautionary Principle (Island Press, 1998).

corporations engage with sustainability experts, policymakers, and industry peers to develop a deeper understanding of the major aspects of the UNGC's framework and how they apply to their specific industries. Furthermore, clarity is progressively enhanced through the UNGC's annual engagements. These engagements serve as a platform for corporations to exchange information, report on their compliance, and refine their sustainability strategies based on evolving best practices. The iterative nature of these engagements allows for continuous clarification, as signatories receive feedback on their sustainability initiatives and adjust their approaches accordingly.

Thus, while environmental standards are often difficult to rigidly define, the UNGC overcomes this challenge by fostering a collaborative learning environment where corporations actively engage in shaping and refining their understanding of sustainability principles. This interactional process ensures that clarity is maintained and continuously strengthened, making the UNGC an effective and adaptable framework for guiding corporate environmental responsibility.

The principles of the UNGC are designed to be ***non-contradictory***. Member corporations can simultaneously uphold all three environmental requirements without facing internal conflicts in their implementation. This coherence is crucial for fostering an integrated approach to corporate sustainability, where businesses do not have to choose between competing obligations but can instead develop holistic strategies that align with all aspects of the UNGC's framework. The three core environmental principles of the UNGC are mutually reinforcing rather than conflicting. For example, a precautionary approach naturally leads to greater corporate responsibility, which in turn fosters innovation in sustainable technologies, thereby creating a positive feedback loop that strengthens a company's overall environmental performance.

This internal coherence is essential for practical implementation, as corporations must be able to integrate these principles without undue or persistent operational inefficiencies or regulatory dilemmas. The UNGC's framework allows for flexibility in execution, enabling companies across various industries to adopt sustainability measures in ways that best suit their sector-specific challenges and opportunities. Additionally, the non-contradictory nature of the UNGC's principles ensures that corporations can maintain regulatory alignment across multiple

jurisdictions. Many multinational corporations operate in diverse legal and regulatory environments, where sustainability obligations may vary. The UNGC serves as a unifying framework that enables companies to adhere to globally accepted environmental principles while complying with local legal requirements, reducing the risk of inconsistencies in corporate sustainability policies. Furthermore, the alignment of these principles enhances corporate governance and strategic planning. By embracing all three requirements cohesively, companies can develop comprehensive sustainability strategies that integrate risk management, CSR, and long-term economic growth. This structural integrity allows businesses to maximize their impact on sustainable development while maintaining regulatory compliance, operational efficiency, and long-term economic viability.

The interactional process through which the UNGC has been developed plays a crucial role in ensuring that compliance with its principles is relatively ***possible and feasible*** for its member corporations. Unlike traditional regulatory frameworks that impose top-down mandates, the UNGC's principles emerge from a dynamic, participatory process where corporations actively engage in shaping sustainability norms. One of the key reasons why compliance is relatively possible is that corporations themselves influence the formation and evolution of these principles. Through continuous dialogue, learning networks, and collective decision-making, corporate participants contribute their expertise and practical insights, ensuring that the principles align with real-world business operations and industry-specific challenges. This bottom-up engagement ensures that sustainability expectations are realistic, adaptable, and conducive to long-term corporate success, rather than being perceived as onerous or impractical regulatory burdens.

Additionally, feasibility arises from the UNGC's network-based approach allowing for flexibility in implementation, recognizing that different corporations operate in diverse industries, legal frameworks, and economic contexts. The voluntary nature of the UNGC does not mean that compliance is optional in practice, but rather that corporations are encouraged to progressively integrate sustainability principles into their strategies at a manageable pace, making incremental improvements over time. This approach enhances long-term feasibility, as businesses can gradually adapt their operations without disrupting financial stability or market competitiveness. Moreover, the collaborative and knowledge-sharing platforms within the UNGC provide

corporations with access to best practices, case studies, and expert guidance. This facilitates the practical implementation of sustainability initiatives, making it easier for corporations to navigate challenges related to environmental responsibility.

By embedding its principles within an interactional process, the UNGC fosters a regulatory environment where compliance is both achievable and beneficial. Businesses are not merely following abstract principles; instead, they are actively involved in a living system of norm evolution, where their contributions shape the very standards that they adhere to. This ensures that the principles remain relevant, adaptable, and aligned with both corporate interests and broader SDGs. Ultimately, the UNGC's interactional approach enhances corporate engagement, facilitates implementation, and ensures that compliance is possible, reinforcing its role as an effective framework for promoting sustainable and responsible business practices worldwide.

Although the UNGC is designed as an evolving framework, continuously adapting to emerging global challenges and sustainability demands, the core objectives of its environmental principles remain ***constant*** over time—even as constancy does not mean an original stasis is required, and deepening and extensions of the principles can make more robust what that core means. Core constancy ensures that member corporations do not face uncertainty regarding the foundational rules and expectations they are required to follow. By maintaining a stable normative foundation, the UNGC allows businesses to develop long-term sustainability strategies without the risk of sudden shifts in environmental obligations that could disrupt corporate planning and investment decisions.

At the same time, the UNGC's procedural structure plays a critical role in preserving shared understandings of the constant core among participants while ensuring that its norm-making (as in, norm deepening, norm concretizing, etc.) process remains transparent and predictable. By striking a balance between evolutionary flexibility and principled constancy, the UNGC provides a stable yet adaptable framework for corporations. This ensures that environmental commitments remain clear, feasible, and aligned with the broader goal of sustainable development, while simultaneously fostering a regulatory culture rooted in collaborative learning, transparency, and predictability.

Finally, the ***congruency*** between the UNGC's environmental principles and their implementation by the UNGC's participants is reinforced through annual CoP reports. These gatherings serve as a crucial mechanism for guiding corporations in effectively integrating UNGC principles into their business operations, ensuring that sustainability commitments translate into tangible corporate practices. By providing a structured forum for dialogue, peer learning, and knowledge exchange, CoP reports help companies navigate challenges, share best practices, and refine their approaches to environmental responsibility. Beyond merely supporting compliance, these annual CoP reports uphold the integrity of the UNGC by fostering a culture of accountability and continuous improvement. They function as a regulatory check-in, ensuring that signatory corporations remain actively engaged in sustainability efforts rather than treating participation as a symbolic gesture. Through transparent reporting and collective scrutiny, the meetings encourage businesses to demonstrate measurable progress, thereby reinforcing the legitimacy and credibility of the UNGC as a global governance framework.

Moreover, the congruence between norm and practice within the UNGC framework encapsulates a broader feature of international law—the necessity of a continuous legality practice among diverse actors. The UNGC's emphasis on recurring engagement, interactive compliance mechanisms, and iterative learning nurtures a growing sense of ethical, sliding into legal, obligation among participants. As corporations regularly assess and refine their sustainability efforts in accordance with UNGC principles, they contribute to the gradual entrenchment of these norms within the global business landscape, strengthening the normative force of corporate environmental responsibility. By ensuring that the principles outlined by the UNGC are not merely aspirational declarations but actionable commitments, this interactional process bridges the gap between soft law and effective governance. Over time, as corporate behaviors align more consistently with these principles, the UNGC's influence expands, shaping global expectations on corporate sustainability and reinforcing the necessity of environmental stewardship as a business imperative.

4.3.4.2.3 Continuous Practice of Legality

The third essential condition for fostering a sense of obligation among participants within the UNGC is the principle of reciprocity—the mutual expectation that all members will adhere to the

UNGC in good faith. Reciprocity serves as a reinforcing mechanism, ensuring that compliance with the UNGC's principles is not merely a voluntary, symbolic gesture but rather an expectation rooted in collective responsibility and normative engagement. Earlier in the discussion, I demonstrated how the community of practice upholds the UNGC framework and how the criteria of legality enable participants to reason with the UNGC's principles through continuous engagement and interactive compliance processes. I have also examined how diverse stakeholders engage in sustained dialogue to establish shared understandings of corporate responsibility and gradually cultivate the normative force of the UNGC's environmental principles.

What remains is whether participants comply with the UNGC's principles and how the continuous practice of legality contributes to fostering a deeper sense of obligation (fidelity) towards environmental commitments. Compliance is not solely a matter of formal adherence but is instead embedded in a self-reinforcing system of peer accountability, reputational incentives, and interactive learning. When corporations see their counterparts actively integrating sustainability into their operations, they are more likely to internalize the principles themselves and perceive non-compliance as a deviation from established norms. In the following section, I will examine the ongoing practice of legality within the UNGC framework as the final step in generating fidelity to its environmental principles, thereby solidifying the UNGC's status as transnationalized customary international law.

Seeking to make a claim regarding the legal status of the UNGC, it is argued that the UNGC will be considered as transnationalized customary international law "when shared understandings become fused with a 'practice of legality', rooted in Fuller's eight criteria of legality and embraced by a community of practice that adheres to those criteria in day-to-day decision-making."[946] The practice of legality within the UNGC largely depends on the reciprocal adherence of participants to its principles, fostering a sustained commitment to its framework, and then generate fidelity to the UNGC. Legality in this context is not merely a formal requirement but a dynamic process that builds and maintains shared legal understandings around the UNGC. Ratifications—becoming members of the UNGC—alone do not suffice; rather, the

[946] Brunnée & Toope, *supra* note 921 at 86.

existence of an active and enduring practice of legality is essential within an interactional framework. The practice of legality thus involves how participants, through repeated contribution and continuous engagement, progressively embed sustainability commitments into their operational strategies, which plays a crucial role in reinforcing the UNGC's legitimacy.

To assess the extent to which the UNGC's principles shape the interests and identities of its participants, I undertake a twofold analysis. First, I examine how signatory corporations actively engage with and implement the UNGC's principles in their operations. Second, I briefly analyze how UN member States incorporate references to the UNGC in their decision-making process, notwithstanding not being direct signatories to the UNGC.

To examine whether corporations actively practice the requirements of UNGC rather than content themselves with merely being signatory members without actual, follow-on commitment, I review *the UN Global Compact 2022 Annual Report,* which states "80% of surveyed companies are implementing the ten principles in their strategies and/or operations" and also "86% of surveyed companies have taken action to advance the SDGs."[947] This level of collective and reciprocal action reinforces the importance of UNGC's principles in advancing the global sustainability agenda and accelerating progress toward the 2030 *Agenda*. See Table 2, extracted from *the UN Global Compact 2022 Annual Report*, for an overview of how much UNGC's principles influence the behavior of participants in different areas of their core business, of their advocacy and communications policy, and of their collaboration with each other.[948]

Table 2: Actions Surveyed that Companies Are Taking to Contribute to the Global Goals.

Core Business
• upholding the ten principles of UNGC: 77% • develop products and/or services that contribute to the goals: 58% • align core business strategy with the goals: 51%

[947] United Nations Global Compact (UNGC), *supra* note 823 at 13.

- set corporate goals that are sufficiently ambitious, science-based and/or align with societal needs (including alignment with SDG ambition benchmarks): 41%
- design business models that contribute to the goal: 36%

Advocacy and public policy

- publicly communicate/disclose their global goals practices and impacts: 45%
- publicly advocate the importance of action in relation to the goals: 35%
- participate in key summits and other important public policy related to the goals: 28%
- advocate for policy alignment with the global goals: 24%
- contribute to country's global goals national action plan: 18%

Collaboration and partnerships

- engage in partnership projects with public or private organizations: 55%
- participate in industry collaboration to advance the goals: 44%

Beyond statistical evidence, several leading multinational corporations exemplify this commitment through concrete actions. The following examples aim at illustrating how corporations are actively embedding the UNGC's principles into their strategies and operations, moving beyond mere membership to demonstrate tangible commitments.

Unilever, a long-standing UNGC's participant, integrates the UNGC's principles into its Sustainable Living Plan, which prioritizes human rights, environmental sustainability, and anti-corruption measures.[949] Regarding the UNGC's environmental principles, Unilever actions are guided by its ambitious sustainability agenda, which focuses on climate, nature, and plastics:

[949] *Unilever Climate Transition Action Plan* (Unilever, 2024) online: <https://www.unilever.com/files/ctap.pdf>.

1) Climate Action: Unilever has a Climate Transition Action Plan (CTAP) with science-based targets to achieve net-zero emissions from its products (from source to point of sale) by 2039.[950]
    - It has delivered a 74% reduction in Scope 1 and 2 greenhouse gas (GHG) emissions since its 2015 baseline, through transition to renewable electricity.
    - It has focused on reducing its Scope 3 emissions from raw materials and ingredients through its Supplier Climate Programme and by transforming its palm oil supply chain.
    - It has launched a €1 billion Climate & Nature Fund to invest in meaningful and decisive action contributing to a net zero world.
2) Nature and Regenerative Agriculture: Unilever is working towards a deforestation-free supply chain by 2023.
    - 97.5% of Unilever's palm oil, paper and board, tea, soy and cocoa order volumes were deforestation-free by the end of 2023, based on Unilever's deforestation-free requirements.
    - Unilever's current regenerative actions already cover a total area of 9m hectares across Latin America, South East Asia, and Africa. Within these regions, it is helping to protect and restore over 200,000 hectares of forests and have a pipeline of projects that would extend to cover a further 300,000 hectares.
    - Unilever sets new goals to implement regenerative agricultural practices on 1 million hectares and to protect and restore 1 million hectares of natural ecosystems by 2030.
3) Plastics and Waste Reduction: Unilever aims to reduce its virgin plastic footprint by 30% by 2026 and 40% by 2028. It also has a goal to make 100% of its plastic packaging reusable, recyclable, or compostable by 2030.
    - Unilever designs lighter packaging and increasing the use of recycled plastic.
    - Unilever explores new paper-based flexible packaging materials and technologies.
    - Unilever runs refill pilot projects globally.

[950] The Science Based Targets initiative is a partnership between CDP, the United Nations Global Compact, World Resources Institute (WRI), and WWF. It aims to catalyze private sector action on climate change by supporting companies and financial institutions to understand how quickly they need to reduce emissions, to align with net zero science-based targets, in line with the more ambitious Paris ambition of limiting warming to 1.5°C.

It should be noted that Unilever has been intensively criticized and accused of being a paradigm example of greenwashing—for example, with respect to plastics.[951] However, while Unilever has faced legitimate criticism over specific marketing practices and the pace of plastic reduction, these concerns represent only part of the broader picture of its move towards sustainable development. Unilever's compliance with climate change mitigation could show its long-term efforts to integrate the UNGC's environmental principles through public reporting, measurable goals, and engagement in global sustainability initiatives. Although the plastic-related critiques raise valid questions, Unilever's extensive sustainability strategy, systemic integration of environmental and social standards support the argument that it remains committed to the UNGC's principles beyond surface-level claims.

Similarly, Ørsted, the Danish multinational energy company, provides a compelling, practical example of a UNGC signatory enacting profound environmental change. A decade ago, the company was one of the most fossil-fuel-intensive utilities in Europe. Today, it is a global leader in offshore wind energy, having fundamentally reshaped its business model.[952] The Ørsted's transition policy is aligned with the UNGC's principles on environmental protection through a set of practical actions:[953]

1) Principle 7: Support a precautionary approach to environmental challenges:
    - Scope 1 greenhouse gas (GHG) emissions decreased by 54% from 2023 to 2024. The main driver was the 53% decrease in the non-renewable fuels used in the heat and power generation, where coal consumption decreased by 62%.
    - Location-based scope 2 GHG emissions decreased by 37% from 2023 to 2024, primarily driven by less purchased power for the electric boilers at our CHP plants
    - Scope 3 GHG emissions increased by 61% from 2023 to 2024.

[951] Julia Kollewe, "Dove and Marmite maker Unilever to be investigated in UK over 'greenwashing'", *The Guardian* (2023), online: <https://www.theguardian.com/business/2023/dec/12/dove-marmite-unilever-investigated-uk-greenwashing>.
[952] *Ørsted: On the path to net zero*, by Knut Bjarn Haanaes & Marc Chauvet (IMD Research & Knowledge, 2022) online: <https://www.imd.org/research-knowledge/sustainability/case-studies/orsted-on-the-path-to-net-zero/>.
[953] Annual report 2024, *Ørsted Annual report 2024* (2025), online: <https://cdn.orsted.com/-/media/annual2024/orsted-annual-report-2024.pdf?rev=02bde37dc8424c8eb8e4e9f3b65cc833>.

- It has systematically decommissioned its coal-fired power plants. The company completely stopped using coal in 2023 and is on track to fully phase out fossil fuels from its heat and power generation by 2025.

2) Principle 8: Undertake initiatives to promote greater environmental responsibility.
    - It takes initiatives such as mangrove reforestation in the Gambia remove carbon dioxide from the atmosphere, supporting efforts to limit global warming to 1.5 °C.
    - In its offshore wind projects, Ørsted is now actively working to achieve a net-positive biodiversity impact. This includes initiatives like creating 3D-printed reefs to support marine ecosystems around turbine foundations.
    - In 2021, it became the first energy company to set a science-based net-zero target covering scope 1-3 emissions by 2040. To provide a more detailed trajectory for its decarbonization efforts, the company developed the Science Based Targets initiative.
3) Principle 9: Encourage the development and diffusion of environmentally friendly technologies:
    - As of 2024, it has installed over 25% of the world's total offshore wind capacity, significantly contributing to the global transition away from fossil fuels and preventing millions of tons of CO2 from entering the atmosphere annually.
    - It has invested billions of dollars in offshore wind farms, which now power millions of homes and businesses across Europe, North America, and Asia.
    - It Builds on existing marine life protections by developing a new lower-noise installation technologies, which strengthens existing protections to marine life.

The practice of legality among the UNGC's participants is also exemplified through their initial letters of commitment and their annual Communication on Progress (CoP) reports. While the letter states the company's intention, the CoP is where the company provides a detailed account of the actions, policies, and outcomes that seek to demonstrate it is putting that intention into practice. These actions are integral instruments that function not merely as procedural or administrative requirements, but as commitment-reaffirmation and norm-development acts. The letter of commitment reflects an initial alignment of participants with the UNGC's principles, while ongoing CoP reporting serves as a form of public signaling of congruence between those

principles and the internal practices of participants. Together, these elements support the idea that the UNGC is developed through practice and legitimacy combined.

Upon joining the UNGC, companies are required to submit a Letter of Commitment signed by their chief executive officer, formally affirming their dedication to the UNGC's ten principles. This serves as a formal declaration of the participants initial alignment with and willingness to uphold the UNGC's principles. This entry-point document not only signifies the participant's endorsement of the UNGC's core values but also marks the beginning of their integration into a broader community of practice committed to responsible and sustainable business conduct. This initial pledge confers upon them the status of "active participant." While it does not show a company's actual practice, it is a critical first step that demonstrates a public and high-level commitment to the UNGC's principles. Its role is to establish a framework of accountability that the company must then fulfill through its subsequent actions.

To maintain this status, companies must regularly disclose how they integrate the UNGC's principles into their corporate policies, operations, and organizational culture through the submission of CoP reports. This is the primary mechanism for a UNGC member company to demonstrate its commitment to and progress on the ten principles. It provides a structured and transparent way for companies to show how they are embedding these principles into their strategies and operations. The CoP reports process is based on the concepts of public accountability and continuous commitment to ensure the credibility of corporations' engagement in the UNGC, confirm corporate responsibility practices, and protect the integrity of the UNGC. It requires companies to communicate annually with stakeholders about the progress made in implementing the ten principles and supporting UN goals through partnerships: "communication to stakeholders (e.g., consumers, employees, organized labour, shareholders, media, government) on the progress the company has made in implementing the ten Global Compact principles and, where appropriate, supporting UN goals through partnerships."[954] The CoP reporting comprises two essential elements:

[954] United Nations Global Compact, *The Practical Guide to the United Nations Global Compact Communication on Progress* (2008), online: <https://www.undp.org/sites/g/files/zskgke326/files/migration/tr/Practical_Guide_2008_En.pdf>.

1. **CEO Statement of Continued Support**: A public affirmation from the company's highest executive, reiterating ongoing commitment to the UNGC's ten principles.
2. **Detailed Disclosure**: A standardized questionnaire that captures the company's performance and progress in areas related to the ten principles and the SDGs.

The focus of these repots is on the subsequent interactions among participants to examine whether a sense of obligation has emerged through the practice of legality. The CoP is not just about stating policies; it requires companies to report on concrete actions and their outcomes. For each principle, the questionnaire asks for details on what the company is doing and the results of those actions. This moves beyond a simple declaration of intent to a demonstration of tangible progress. Companies may provide quantitative data, case studies, and examples of initiatives they have implemented. In these reports, signatory companies of UNGC, in order to be considered active participants, must:

- Express their continuing support and ongoing commitment to the UNGC and its ten principles.
- Describe their practical actions taken to implement the ten principles or an explanation if they have not acted in any particular area.
- Explain a measurement of outcomes to demonstrate to what degree their targets/performance have been met.[955]

Accordingly, failure to submit the CoP reports within the specified timeframe results in a change of status to "non-communicating," and prolonged non-compliance can lead to de-listing from the UNGC.[956] Through this de-listing procedure, the UNGC seeks to maintain the practice of legality among participants by requiring corporations to implement UNGC's principles and participate in UNGC activities. Since its emergence, 15,928 members have been removed from the UNGC list of participants for failure to communicate progress. Despite the large number of companies removed from the participant list, the overall number of participants that are all complying with UNGC's principles continues to rise. This rigorous reporting process not only holds

[955] Find detailed information on the requirements of CoP and the listing/delisting proves, *see* "The UN Global Compact and Human Rights" (2017), online: *SDG Resource Centre* <https://sdgresources.relx.com/legal-practical-guidance/un-global-compact-and-human-rights>.
[956] "Reporting | UN Global Compact", online: <https://unglobalcompact.org/participation/report>.

corporations accountable but also encourages continuous improvement and alignment with global sustainability objectives. By actively submitting in the CoP reports, companies demonstrate their commitment to ethical practices, environmental stewardship, and social responsibility, thereby reinforcing the UNGC's mission to promote sustainable and responsible business practices worldwide.

To analyze how UN member States incorporate the UNGC in their decision-making process, I first analyze international investment agreements that refer to the UNGC as well as documents related to the UNGC that host States submit to investment tribunals during the investment dispute procedures. This trend highlights how the UNGC is being integrated into the core of global governance frameworks. By examining governmental engagement, it becomes clear that the UNGC is far more than a symbolic initiative; it is a dynamic and influential framework that actively shapes regulatory landscapes across a range of sectors. As such, it plays a critical role in reinforcing the legitimacy and legal standing of the UNGC, ensuring its continued relevance and impact in the global governance of sustainability and corporate responsibility. This evolving practice suggests a broader commitment to responsible business conduct and sustainable development, emphasizing the UNGC's growing role in setting international norms and expectations.

References to the UNGC are sometimes found in the preamble of international investment agreements/model treaties, which—taken together with the other evidence—is a signal of the practice of legality among States. For example, the model treaty elaborated by Austria mentions that the contracting parties are "TAKING NOTE OF the principles of the UN Global Compact."[957] In Free Trade Agreement Between the EFTA States and Montenegro, the parties acknowledge good corporate governance and corporate social responsibility for sustainable development by observing:

> Internationally recognized guidelines and principles in this respect, such as the OECD Guidelines for Multinational Enterprises, the OECD Principles of Corporate Governance and the UN Global Compact.[958]

[957] note 884.
[958] note 885 at IV.

Likewise, the Comprehensive Economic Partnership Agreement between Indonesia and the European Free Trade Association, in its preamble, mentions that the parties:

> [acknowledge] the importance of good corporate governance and corporate social responsibility for sustainable development, and [affirm] their aim to encourage enterprises to observe and adhere to internationally recognized guidelines and principles in this respect, such as the OECD Guidelines for Multinational enterprises … and the UN Global Compact.[959]

The Comprehensive Enhanced Partnership Agreement between the European Union and Armenia, in Article 276 on trade and investment favoring sustainable development, confirms parties' commitment to enhance the contribution of trade to the goal of sustainable development in its economic, social and environmental dimensions. To that end, the Parties:

> (e) agree to promote corporate social responsibility, including through the exchange of information and best practices. In that regard, the Parties refer to the relevant internationally recognized principles and guidelines, such as the OECD Guidelines for Multinational Enterprises, the UN Global Compact and the ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy of 1977.[960]

Article 31 of the model treaty elaborated by Norway in 2015 focuses on the encouragement of investors to consider specific informal instruments:

> The Parties agree to encourage investors to conduct their investment activities in compliance with the OECD Guidelines for Multinational Enterprises, the UN Guiding Principles on Business and Human Rights and to participate in the United Nations Global Compact.[961]

In the ASSOCIATION AGREEMENT between the European Union and the European Atomic Energy Community and their Member States, of the one part, and the Republic of Moldova, of the other part, the Parties reconfirm their commitment to enhance the contribution of trade to the goal of sustainable development in its economic, social and environmental dimensions. Accordingly, the Parties:

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[959] *Comprehensive Economic Partnership Agreement between the Republic of Indonesia and the EFTA States* (2018), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5802/download>.
[960] *Comprehensive and Enhanced Partnership Agreement between the European Union and the European Atomic Energy Community, and their Member States, of the One Part, and of the Republic of Armenia, of the Other Part* (2017), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/5669/download>.
[961] *Agreement between the Kingdom of Norway and ___for the Promotion and Protection of Investments* (2015), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3350/download>.

> agree to promote corporate social responsibility, including through the exchange of information and best practices. In that regard, the Parties refer to the relevant internationally recognised principles and guidelines, such as the OECD Guidelines for Multinational Enterprises, the United Nations Global Compact, and the ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy.[962]

The ASSOCIATION AGREEMENT between the European Union and their Member States, of the one part, and Ukraine, of the other part, states that the Parties shall strengthen their dialogue and cooperation on promoting the decent work agenda, employment policy, health and safety at work, social dialogue, social protection, social inclusion, gender equality and non-discrimination. To this end, it notes that:

> the parties shall promote corporate social responsibility and accountability and encourage responsible business practices, such as those promoted by the UN Global Compact of 2000, the International Labour Organization (ILO) Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy of 1977 as amended in 2006, and the OECD Guidelines for Multinational Enterprises of 1976 as amended in 2000.[963]

Further contribution to the evidence of a practice of legality around the UNGC arises from its invocation by host States in investment disputes as well as ISDS tribunals' reliance on the UNGC in their reasonings. It should be mentioned here that although future ISDS tribunals are not legally obligated to follow earlier decisions on the use of the UNGC, there has long been both a scholarly and a real-world understanding of the high relevance of previous decisions. Such relevance is not just because of potential persuasive substantive value (to the extent there are robust reasons given, which admittedly is often not the case in the civil law world) but also they are given weight—that amounts to precedential force—in more sophisticated civil-law thinking through the notion of *jurisprudence constante*, consistent decisional case law.[964] In the following,

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[962] *Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and the Republic of Moldova, of the other part* (2014), online: <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3125/download> Article 367.
[963] *Association Agreement between the European Union and its Member States, of the one part, and Ukraine, of the other part* (2014), online: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:22014A0529(01)> Article 422.
[964] *Jurisprudence constante*, consistent decisional case law, in civil law differs from common-law precedent in the sense that it needs an accumulation and solidification of at least several decisions and courts/tribunals cannot just treat something as precedent because it was said by single a parallel or hierarchically superior court/tribunal. In addition, it is a mistake to ignore the fact that the International Court of Justice's statute makes clear that the two leading sources of law that do not emanate directly from the (political) State—the writing of publicists (revered in the civil law world) and the decisions of courts (revered in the common law world)—are nonetheless treated as subsidiary/indirect sources in the ICJ Statute in a way that requires more sophistication in references to and discussion of those writings and decisions than can be captured by saying in on/off terms that they are formally non-

I explain that the decisions of ISDS tribunals referring to the UNGC are signals for the continuous practice of legality among the UNGC's member states to foster a deeper sense of obligation (fidelity) towards environmental commitments. And such practice of legality signals that the UNGC represents a source of obligations for investors and are not simply treated as if they are one-off applications of no relevance to the evolution of the overall body of law.

During the investment dispute procedures in *Copper Mesa Mining Corporation v. Republic of Ecuador*, the respondent State invoked the UNGC to challenge the jurisdictional competence of the tribunal on the ground that the investment made by the claimant was tainted with illegality. The host State contended that the claimant's investment was made in a manner not in accordance with not only the laws of Ecuador but also international law. In brief, the respondent submitted that:

> even assuming that the Claimant had made investments in Ecuador, those investments are tainted by illegality under both Ecuadorian law and public international law, arguing that the concessions were acquired on the basis of illegally obtained information and that they were illegally awarded and illegally transferred to the Claimant. Moreover, the conduct of the Claimant's alleged subsidiaries, as well as that of its agents and employees, amounts, so the Respondent submits, to severe breaches of legal principles governing corporate social responsibility and is contrary to international public policy, including the UN Global Compact, the OECD Guidelines and the Voluntary Principles.[965]

The tribunal rejected the jurisdictional challenge raised by the host State and noted that the illegality of the investment at the establishment stage must be assessed in accordance with the national law of the host State. The tribunal confined the assessment of jurisdictional competence to the legality of the investment's establishment under national law of the host State.[966] However, the tribunal's silence on the status of the UNGC does not equate to a rejection of it as a rule of law. Indeed, it did not preclude the relevance of international norms in other contexts or at other stages of legal analysis: the tribunal agreed with the host State's argument that the claimant's "flagrant breaches of international human rights law and international public policy," particularly during the

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binding, Rodrigo Camarena González, "From Jurisprudence Constante to Stare Decisis: The Migration of the Doctrine of Precedent to Civil Law Constitutionalism" (2016) 7:2 Transnational Legal Theory 257–286.

[965] *Copper Mesa Mining Corporation v. Republic of Ecuador, supra* note 235 para 5.29. Later in its defence, the host State made a distinction between public policy and international law: "The Respondent further contends that these concessions were also not operated in accordance with Ecuadorian law as the Claimant engaged in a series of unlawful activities violating Ecuadorian law and international law, as well as international public policy," *Ibid* para 5.30. The host State also clarified that the illegality of claimant's conduct is due to either to (1) the claimant's own internationally illegal conduct or 2) conduct that is incompatible with international public policy: *Ibid* para 5.39.

[966] *Ibid* para 5.54.

post-acquisition period, could render the claimant's claims inadmissible. The tribunal went on to refrain from dismissing the claimant's claim on the basis of breach of law or public policy, on the basis both that the claimant's action did not constitute a serious violation of human rights law and that the host State did not present these arguments before the arbitration began. But the tribunal then joined what remained of the host State's admissibility case related to breaches of law and public policy to the merits of the claimant's claims. At the merit stage, the tribunal accepted the relevance of the claimant's misconduct based on contributory fault, while limiting its findings about such misconduct to the affront to international and national public policies of the host State—thereby ultimately sidestepping an assessment of whether there was (also) a direct breach of international legal obligations by the company.[967] Significantly, though, the result of its law-infused understanding of public policy was significant. As a result of this, the tribunal reduced the compensation awarded to the claimant by 30%, attributing this portion of the loss to the company's own misconduct.[968]

The UNGC was also explicitly invoked by *amicus curiae* in *Piero Foresti, Laura de Carli et al. v. Republic of South Africa (2009)* case. The petitioners were all public interest organisations who sought to assist the tribunal in its resolution of the dispute by raising and discussing relevant human rights-related issues and legal obligations arising within the scope of the dispute. To explain the human rights and sustainable development dimensions of the dispute that make the dispute of public interest to the international community at large, the petitioners submitted that the tribunal must take into consideration the international human rights law obligations of both the host State and the investor. In particular, the petitioners highlighted the investor's international responsibilities in respect of human rights, labour rights, and environmental protection by invoking principles 1-9 of the UNGC and pointing out "the concomitant international responsibility of investors to contribute to human rights fulfilment, environmental protection, and the social upliftment of affected workers and communities when exploiting a nation's natural resources."[969] The petitioners then requested to contribute constructively to the proceedings by providing unique perspectives on these legal dimensions of public interest issues.

[967] *Ibid* para 5.65.
[968] *Ibid* para 7.30.
[969] *Piero Foresti, Laura de Carli et al v. Republic of South Africa,* ICSID Case No ARB(AF)/07/01, Petition for Limited Participation as Non-Disputing Parties, Award 17 July 2009, para 4.

Although the tribunal did accept the restricted involvement of the petitioners in the proceedings, in its own judgment it did not comment on the petitioners' invocation of the UNGC.[970]

Most importantly, amidst the submissions from host States and *amicus curiae*, the ISDS tribunal in the *Urbaser* case relied upon the content of the UNGC to address the conduct of investors and to acknowledge the emergence of investors' responsibility to respect human rights.[971] In *Urbaser*, the host State articulated its plea of the post-establishment illegality defence and then initiated a counterclaim based on damages that it suffered and that allegedly resulted from the investor's non-compliance with obligations under the UNGC: "It is a fundamental right that the leading companies of the world have adopted in the Global Compact as being part of their corporate social responsibility."[972] The host State then argued that it is evident that rules of international human rights law create obligations that must also be respected by multinational companies. When assessing the host State's defence and merits of its counterclaim, the tribunal recalled the references to several informal instruments, including the UNGC, by the host State with a view to conveying an understanding of human rights recognized in international law as binding upon business enterprises.

The *Urbaser* tribunal acknowledged that instruments generated by corporations themselves , such as the Global Compact, can concretize a corporation's obligations as they relate to human rights.[973] It is therefore to be admitted by the tribunal that "the human right for everyone's dignity and its right for adequate housing and living conditions are complemented by an obligation on all parts, public and private parties, not to engage in activity aimed at destroying such rights." Even if the counterclaim was ultimately dismissed due to the tribunal in *Urbaser* adopting a relatively cautious approach to the category of obligations placed directly on companies by international human rights law, that tribunal's foundational holding that the UNGC is bound up in the customary obligations of companies contributes to the elaboration of

[970] *Piero Foresti, Laura de Carli and others v. Republic of South Africa,* ICSID Case No ARB(AF)/07/1, Award 8 August 2010, para 27-29.
[971] *Urbaser SA and Consorcio de Aguas Bilbao Bizkaia, Bilbao Biskaia Ur Partzuergoa v. The Argentine Republic,* ICSID Case ARB/07/26, Award 8 December 2016, *supra* note 3.
[972] *Ibid* para 1161.
[973] *Ibid* para 1161.

the practice of legality according to which the UNGC can be invoked in future cases to impose human rights obligations on foreign investors.

The inclusion of the UNGC in various investment treaties signifies a growing trend among States to endorse environmental responsibilities of investors within formal legal frameworks. While these references are often included in the preamble of the treaties and/or employ language such as "encourage" or "promote," which suggests a voluntary approach, such inclusion indicates the continuous practice of legality among UN member States. The invocation of the UNGC in the proceedings of investment disputes likewise signal the legality of the UNGC. Although the tribunals, in these cases, remain silent on the status of the UNGC, such invocations could be an indicator of the shared understandings among participants towards the UNGC. Of course, based only on these investment treaties and disputes, we cannot come to a conclusion that the UNGC has acquired the status of transnationalized customary international law, but they do signal a sense of obligation among participants, which is a major step towards endorsing the legality of the UNGC. Legality for the UNGC is not merely a formal requirement but a dynamic process that builds and maintains shared legal understandings around the UNGC.[974] Progressively

[974] While the focus of these examples is the international level, evidence of the evolution of a sense of obligation within a dynamic process can also be found in the growing practice of governments reference the UNGC in their corporate social responsibility policies, public procurement standards, and sustainability regulations. For instance, the European Union's Corporate Sustainability Due Diligence Directive (CSDDD) aligns closely with the UNGC principles, requiring companies to conduct human rights and environmental due diligence across their supply chains, "The Corporate Sustainability Due Diligence Directive (CSDDD) - Directive (EU) 2024/1760", online: <https://www.corporate-sustainability-due-diligence-directive.com>. This directive requires large corporations to identify, prevent, and mitigate adverse human rights and environmental impacts resulting from their operations, subsidiaries, and value chains. By embedding these responsibilities into corporate governance, the CSDDD represents a significant step toward treating the UNGC's principles as binding transnational legislation, aiming to enhance corporate accountability and promote sustainable development. Also, several European countries have integrated the principles of the UNGC into their National Action Plans (NAPs) on Business and Human Rights, thereby embedding these principles into their legal and regulatory frameworks. For example, Denmark published its first NAP that underscores Denmark's commitment to aligning national policies with international human rights standards, reflecting the core values of the UNGC, "Denmark", online: *National Action Plans on Business and Human Rights* <https://globalnaps.org/country/denmark/?utm_source=chatgpt.com>. Denmark's NAP emphasizes the responsibility of businesses to respect human rights and outlines the state's duty to protect these rights, ensuring that corporate activities do not infringe upon them. Germany's NAP also aims to improve the global human rights situation and impart a social dimension to globalization, in line with the *2030 Agenda for Sustainable Development*. In its *National Action Plan: Implementation of the UN Guiding Principles on Business and Human Rights*, Germany highlights its strong support for the UN Guiding Principles on Business and Human Rights and welcomes the efforts to set up substantive National Action Plans, "National Action Plan: Implementation of the UN Guiding Principles on Business and Human Rights", online: *Homepage Business & Human Rights* <https://www.csr-in-deutschland.de/EN/Business-Human-Rights/NAP/About-the-NAP/Original-version-of-the-NAP/art-original-version-of-the-nap.html?utm_source=chatgpt.com>. Germany's NAP outlines expectations for German companies to conduct human rights due diligence and establishes mechanisms to monitor compliance, thereby reinforcing

embedding sustainability commitments into investment treaties plays a crucial role in reinforcing the UNGC's legitimacy. Whatever the softness of the expression of States' own duties to regulate corporations, the key is that States in these treaties are endorsing documents or instruments, including the UNGC, that place direct obligations on corporations. Rather than assuming the softness of the language of the duties on States (to regulate) somehow gets translated to the UNGC in a way that waters down the commitment, it makes more logical and principled sense to say that the structure of these treaty clauses is actually to emphasize that the hard obligations are found within the cited instruments and that it is the addressees of those instruments who must be directly accountable—with States having less onerous obligations in relation to what corporations fail to do in compliance with a cited instrument like the UNGC (again, to promote or encourage compliance).

4.4 Take-Away on the Relevance and Applicability of the UNGC as a rule of Transnationalized Customary International Law in Post-Establishment Illegality Defence

In this chapter, following the explanation of post-establishment illegality defence as a potential avenue to hold foreign investors environmentally responsible in ISDS tribunals, I engaged in the case study of the UNGC to demonstrate the conditions under which host States could invoke its principles as liability law. The relevance of the UNGC as transnationalized customary international law is definitely contingent on the dispute and the particular investment treaty involved. According to the moderate systemic interpretation approach, which is preferred in this dissertation, ISDS tribunals cannot easily accept or reject the UNGC in the treaty interpretation process. Instead, they have to assess the sameness of subject matter of the UNGC in accordance with the treaty involved in the dispute. This assessment must be conducted in accordance with: 1) subject and purpose, 2) context and topic, and 3) value compatibility among the involved treaty and the UNGC. It is also true, when ISDS tribunals determine consistency or inconsistency among the UNGC and the involved investment treaty, such determination cannot occur in the abstract. Rather, it has to be done based on the case-specific question on whether or not the

corporate accountability. These initiatives not only align national policies with international standards but also provide clear frameworks for businesses to operate ethically and sustainably.

rule(s) of the involved investment treaty clearly derogate from the UNGC. Applicability of the UNGC is also dependent on whether ISDS tribunals acknowledge the hybridity of the institutional aspect and the interactional process of the normative dimension of the UNGC in order for the transnational self-regulatory norms associated with it to acquire the legal status of transnationalized customary international law.

Building upon my earlier works, this chapter underscores the relevance and applicability of the UNGC for resolving substantive aspects of investment disputes—especially those with an environmental dimension. This reveals a largely untapped potential for the UNGC to be recognized as transnationalized customary international law and then be treated as substantive law in investment disputes. Such potential offers a pragmatic and effective means to strike a balance between the rights and obligations of foreign investors by placing binding international/transnational environmental obligations directly upon foreign investors.

To better illustrate how investment protection standards can intersect with environmental obligations by the means of transnationalized customary international law, I conclude this chapter with a hypothetical case study highlighting the evolving role of the UNGC in investor-state dispute settlement procedures.

In this scenario, a foreign cement manufacturing company invests in a developing country and establishes a large cement plant. Cement production involves burning coal and limestone at very high temperatures, releasing significant amounts of sulfur dioxide (SO_2), nitrogen oxides (NO_x), and particulate matter into the atmosphere. Over time, the SO_2 combines with atmospheric moisture to form acid rain, which seeps into local rivers, groundwater, and agricultural lands. This contamination not only acidifies water sources but also mobilizes toxic heavy metals (such as mercury and lead) from soils into the water supply. To limit air pollution, water contamination, and social impact of this investment, the host State imposes regulatory measures to restrict cement manufacturing activities. These limitations, though aimed at reducing air pollution, preventing secondary water pollution, and protecting vulnerable communities disproportionately affected by the environmental harm, significantly undermine the long-term financial viability of the investment.

The investor initiates arbitration before an ISDS tribunal, alleging that the host State's conduct constitutes a breach of the investment protection standards included in the investment treaty. In particular, the investor contends that the host State's measures were arbitrary and disproportionate, claiming they lacked a coherent national policy rationale and were inconsistent with prior state practice. The investor further argues that it had legitimate expectations that the host State's regulatory framework would permit such investment activities, and that it made its investment in reliance on those expectations. Moreover, the investor asserts that it fully complied with all local environmental regulations in force at the time of investment and throughout its operations. On this basis, the investor argues that any subsequent restrictions imposed by the host State for alleged environmental harms amount to a violation of the fair and equitable treatment (FET) standard under the treaty. Consequently, the investor seeks compensation for the host State's alleged breaches of its treaty obligations.

The host State counters by invoking a post-establishment illegality defence, asserting that the investor's operations violated its international environmental responsibilities imposed by the UNGC's environmental principles. Specifically, the State provides evidence that the investor failed to encourage the development and diffusion of environmentally friendly technologies as required by Principle 9. The investor deliberately opted against installing industry-standard flue-gas desulfurization units (scrubbers) on its factory smokestacks—a technology used universally to protect the environment by removing sulfur dioxide (SO_2) from industrial exhaust gases, primarily from power plants that burn coal or oil—to cut operational costs, resulting in excessive sulfur dioxide emissions that caused acid rain and damaged local crops.

Furthermore, the State argues that the investor knowingly disregarded water pollution, directly contravening Principle 8, which calls for greater environmental responsibility. Instead of buffering water and soil (adding calcium carbonate to soils and water bodies) to neutralize acidity and prevent the mobilization of heavy metals into groundwater and rivers, the investor discharged water contamination caused by the cement manufacturing. This prioritization of cost reduction over environmental responsibility directly contributed to the widespread ecological harm and public health crisis.

In its defence, the host State also highlights the investor's breach of Principle 7, the precautionary approach, by the investor failing to conduct a comprehensive environmental impact assessment (EIA) before significantly scaling up its production activities. The State provides evidence that the investor's "assessment" completely bypassed the procedural requirement of consulting with the local communities, who would be most affected by water contamination. By refusing to properly conduct EIA before acting, the host State argues the investor chose willful ignorance over precaution, directly violating the UNGC. The host State then seeks to either make the investor's claim inadmissible because of the investor's international illegal conduct or, alternatively, to exonerate itself from paying full compensation because the investor's ongoing operation is characterized by illegal conduct.

To resolve the dispute, the investment tribunals is required to interpret the investment treaty in accordance with "the relevant rules of international law applicable in the relations between the parties". By using the doctrinal and theoretical findings of this dissertation, the tribunal would treat the UNGC as a source of liability norms that is both relevant and applicable to the substantive aspects of the case. Incorporating the UNGC's environmental principles into the legal reasoning of the ISDS tribunal would confirm that compliance with internationally recognized sustainability standards forms part of the investor's broader obligations. The tribunal would then emphasize that investors cannot invoke treaty protections while simultaneously disregarding their environmental obligations imposed by transnationalized customary international law, particularly when such misconduct directly necessitates the regulatory measures being challenged. To decide on the post-establishment illegality conduct of the investor due to violations of its international obligations, the tribunal would refer to the clean hands doctrine (no one can be heard to invoke his own turpitude) to decide on the admissibility of the claim and/or the merits of the dispute. As a result, the tribunal could either dismiss the investor's claim as inadmissible or, alternatively, reduce the compensation awarded to the investor in light of their non-compliance with environmental obligations.

In doing so, the tribunal would aim to protect environmental interests on an equal footing with investment protection, ensuring that investor protective rights are upheld alongside their

environmental responsibilities**.** This balanced approach reinforces the notion that international investment law would advance the realization of *the 2030 Agenda for Sustainable Development*, an objective central to this dissertation.

Concluding Pathways

Holding foreign investors environmentally accountable under current law has been the core objective of this dissertation. Achieving this objective, however, necessitates a balanced consideration of both the rights and responsibilities of foreign investors within the framework of investor–state dispute settlement (ISDS) tribunals. The central argument of this study has revolved around the paramount importance role of transnational self-regulatory norms imposing environmental obligations on foreign investors in achieving such a balanced approach, particularly in conjunction with investment agreements at issue before ISDS tribunals. Nonetheless, recognizing and giving effect to such norms faces significant theoretical and practical challenges, and their effective incorporation into the dispute settlement process requires meeting a clearly defined set of criteria.

This dissertation's central argument rests on the foundation established in Chapter 1. Through an in-depth literature review and case law analysis of the ISDS system, the chapter demonstrates how tribunals have historically prioritized investor protections, often at the expense of States' sovereign rights to enact environmental regulations: while ISDS tribunals were created to protect investors, the interpretation of investor rights by these tribunals has, for many decades now, evolved to the point of often impeding environmental protection measures taken by host States. The analysis disclosed this system disproportionately favors investor rights, thereby creating an urgent need for analysis as to the extent to which current law allows imposing environmental obligation on investors too. Chapter 1 identifies a critical tension in global investment governance but also a crucial point of departure: the *Urbaser v. Argentina* case. While its direct jurisprudential impact has been limited so far, *Urbaser* opened a vital conceptual door by acknowledging both that investors could bear obligations directly under international law and transnational self-regulated norms could be used in the dispute settlement procedures. These decisive ideas—that an investor's role might extend beyond that of a rights-holder and that rules of international law external to investment treaties could be used in the dispute resolution process—provided the essential premise to be investigated and explicated in the analysis developed across the remainder of this dissertation.

Building on this conceptual opening, the argument then turned to a core challenge: how may ISDS tribunals systematically engage with transnational self-regulated norms, such as those imposing environmental obligations on foreign investors? Chapter 2 addresses this doctrinally. It delves into the interpretive rules of international law, discussing how the Article 31(3)(c) of the Vienna Convention on the Law of Treaties (VCLT) introduces systemic interpretation approach for considering customary norms during treaty interpretation. On the understanding of the contours (including limits) of systemic interpretation that I developed in Chapter 2, this approach seeks both to avoid contradictions between rules from different areas of international law and to respect the intentions of the parties who have entered into specific international agreements. Even while recognizing investment law as a distinct, specialized regime with its own normative boundaries, relevant transnational norms can benefit from a balanced and nuanced integration into investment treaties in a way that allows more robust and extensive consideration of foreign investors' environmental responsibilities than dominant ISDS tribunal practice to date has been willing to undertake. By means of doctrinal analysis, the chapter offers a two-step analytical test to determine if an external norm—such as a transnational self-regulated norm—qualifies as a relevant rule in interpreting and applying a treaty in accordance with Article 31(3)(c) VCLT standard for systemic integration of external rules ("any *relevant* rules of international law applicable in the relations between the parties"—my emphasis added). This relevance test, which assesses both the sameness of subject matter and the consistency between the norm and the treaty, provides a structured yet flexible systemic interpretive guideline for arbitrators. In doing so, it constructed the necessary legal bridge for ISDS tribunals to systematically connect the rights included in an investment treaty with the responsibilities imposed by transnational self-regulated norms.

The next key inquiry is to determine the applicability of such norms, as required under Article 31(3)(c) of the VCLT—"any relevant rules of international law *applicable* in the relations between the parties" (my emphasis added). This requirement needs to theoretically examine the lawmaking authority of non-state actors and recognize the legal status of non-state-based norms in order to be considered as a rule of international law that generates obligations applicable to foreign investors and owed to host States. For this purpose, Chapter 3 examines the institutional and normative aspects of transnational norms with a view to determining their capacity to be

treated as transnationalized customary international law. Hybridity theory along with interactional theory set the scene for understanding this lawmaking phenomenon at the transnational level, where non-state actors join States to develop rules of law through a continuous interactional process. Transnational self-regulated norms can be institutionalized when State and non-state actors cooperate to develop norms that aim to both protect justice and promote efficiency in the relations between various kinds of actors and in a way that parcels out rights and obligations as appropriate to the transnational nature of the subject-matter and associated activity. These norms emerge sociologically but then are legally legitimized (crystallize into) when practice adheres to a set of "criteria of legality" to a sufficient extent that the subjects, who have participated creating the norms, reciprocally fulfill duties while signaling by the practice of legality a sense of obligation to respect the norms.

The dissertation's argument culminated in Chapter 4, where the doctrinal and theoretical frameworks were operationalized through a detailed case study of the United Nations Global Compact (UNGC). This chapter serves to operationalize the entire dissertation by examining whether the UNGC, a prominent complex of transnational self-regulated norms, imposes environmental legal obligations on investors that could be used in ISDS tribunals to hold foreign investors environmentally accountable. The analysis demonstrated that the UNGC (as transnationalized customary international law, stemming from the evolution of the meaning of the instrument's text through years of interpretation and implementational practice) has the clear potential to be recognized by tribunals as a source of international law that is relevant and applicable for treaty interpretation. This concluding step helps demonstrate that the dissertation is not merely an abstract construct but a practical framework with real potential for ensuring investors can reasonably be held environmentally accountable through the coalescing of not only rights but also responsibilities of foreign investors in ISDS tribunals. This final chapter solidifies the dissertation's central claim: that there is a practically, theoretically, and doctrinally sound pathway for integrating investors' international obligations into investment arbitration, making environmental accountability of foreign investors not just a conceptual possibility but indeed a legally achievable one.

I end this concluding part by observing, as a kind of epilogue, that the arguments in this dissertation position it as an active scholarly contribution that engages directly with the most recent and significant developments in the field of international climate change litigation. Notably, as this work was being finalized and prepared for defence, the International Court of Justice issued its long-awaited Advisory Opinion on the obligations of States in relation to climate change.[975] While a comprehensive examination of the just-released Advisory Opinion lies beyond the scope of this dissertation and remains a subject for future research, the Court's reasoning—addressing the existential threat of climate change, the importance of systemic interpretation, the role of climate change principles in fostering international environmental accountability, and the imperative for action at individual, societal, and political levels—resonates strongly with the core arguments advanced in this dissertation. This Advisory Opinion opens a fertile and timely avenue to apply the analytical framework developed in these chapters to a rapidly evolving legal landscape surrounding climate change litigation.

Most critically, given the recent controversies surrounding climate change, and in light of the reluctance of certain States—most notably the United States—to fully commit to ambitious climate action, the International Court of Justice's Advisory Opinion explicitly acknowledges climate change as an existential threat that must be addressed within the framework of international law. This affirms the central argument of the dissertation on the urgency of integrating environmental norms of customary international law into the legal interpretation of investment treaties in order to preventing transboundary environmental harms while promoting transnational investment flows. The court then clarifies that to exclude the external rules of international law for treaty interpretation, there must be some actual inconsistency between them, or else a discernible intention that one provision is to exclude the other. Such interpretive approach resembles the one taken in this dissertation to show that, there is, in particular, no indication that investment treaties are meant to apply while simultaneously excluding environmental norms of customary international law. Furthermore, the court is of the view that certain guiding principles such as sustainable development, common but differentiated

[975] *Obligations of States in Respect of Climate Change,* International Court of Justice (ICJ), Advisory Opinion 23 July 2025, *supra* note 110. This judgment has been engaged alongside my supervisor, Professor Scott, who has also consulted the judgment in order to advise on possible implications for the dissertation and post-dissertation work. The passages that follow reflect and in places distill Professor Scott's contributions arising from that discussion.

responsibilities and respective capabilities, and the precautionary approach guide the interpretation of climate change treaties and the determination of rules of customary international law.

Most importantly, the court upholds that the primary responsibility for climate change action rests with States and the private actors under their jurisdiction. These findings carry significant implications for ISDS tribunals. The court emphasizes that States may be held responsible for failing to take necessary measures to limit the quantity of emissions caused by private actors under its jurisdiction. This unequivocally includes an obligation to limit emissions caused by foreign investors, including fossil fuel companies. The kinds of regulatory actions clearly contemplated by the International Court of Justice as falling within the positive international legal obligation of States to regulate private actors' emissions are likely to prompt foreign investors to initiate disputes before ISDS tribunals as they have been doing for years now. However, challenging the environmental measures adopted by host States as having adverse (and compensable) economic impacts on their investment activities will be faced now with a very different juridical field. The entire International Court of Justice's judgment will provide a rejuvenated basis for host States to defend themselves from investor claims by pointing to their duties (most generally, but also most powerfully, the duty of due diligence) as generating a positive obligation to regulate and respond to harmful corporate behaviour—and this will surely put normative pressure on ISDS arbitrators to consider ways to preclude or mitigate the wrongfulness of state regulation that is mandated (not just permitted) by international law's duty of due diligence and associated positive duties. Much will depend on how much ISDS tribunals insist on reading a given investment treaty as in conflict with the general climate change obligations and thus preferring investment protection over climate protection—keeping in mind that the court nowhere said that state duties under international climate change rules have evolved to the point of being *jus cogens* norms that would allow application of conflicting investment treaty provisions to be suspended.

With respect to the question of (a) transnationalized (b) customary international law that can place direct duties on private actors, the court does not address this possibility. The questions posed to it by the General Assembly ask only about States' obligations and the law that generates

such obligations and the long set of preambular paragraphs all emphasize only interstate treaties or instruments—and the court's general practice has always been to not overshoot the scope of advisory questions. For this reason, the responsibility of private actors is almost non-existent and, to the extent it is there, it is a refracted presence in the judgment: private activity causing climate change harms is acknowledged throughout but the sole question the court saw itself as charged with answering is what obligations States have to either prevent or respond to such harm. In other words, indirect responsibility of the classic sort in the law of state responsibility (wherein a state is responsible for its own failures or omissions when it has a duty to regulate a private actor) is the order of the day. One can see this distilled at one point in this paragraph where the court responds to a seriously argument that private actions have to be attributable as state actions in order for States to incur responsibility in relation to such private actions:

> Some participants also argued that the conduct of private actors resulting in emissions of GHGs is not attributable to States. In relation to private actors, the Court observes that the obligations it has identified under question (a) include the obligation of States to regulate the activities of private actors as a matter of due diligence. Therefore, attribution in this context involves attaching to a State its own actions or omissions that constitute a failure to exercise regulatory due diligence. In such circumstances, the question of attributing the conduct of private actors to a State does not arise. The legal standard to assess compliance with the obligation to regulate, as well as the nature of the actions or omissions that lead to attribution, has been set out by the Court in several cases (Pulp Mills on the River Uruguay (Argentina v. Uruguay), Judgment, I.C.J. Reports 2010 (I), pp. 79-80, para. 197; United States Diplomatic and Consular Staff in Tehran (United States of America v. Iran), Judgment, I.C.J. Reports 1980, p. 31, para. 63). Thus, a State may be responsible where, for example, it has failed to exercise due diligence by not taking the necessary regulatory and legislative measures to limit the quantity of emissions caused by private actors under its jurisdiction.[976]

There appears to be only one place in the main judgment where direct international law obligations on private actors are mentioned—albeit elliptically—as a feature of some areas of international sustainable development or environmental law:

> Some participants suggested that the principle referred to as "polluter pays" is part of the applicable law. This principle is not mentioned in the climate change treaties but is expressed in Principle 16 of the Rio Declaration, according to which:
> "[n]ational authorities should endeavour to promote the internalization of environmental costs and the use of economic instruments, taking into account the approach that the polluter should, in principle, bear the cost of pollution, with due regard to the public interest and without distorting international trade and investment".

[976] *Ibid* para 428.

> That recommendation has been followed by States in certain sector-specific treaties and various types of national legislation, mostly in the form of strict liability of private actors for specific hazardous activities. However, the principle "that the polluter should, in principle, bear the cost of pollution" is not envisaged or reflected in any of the climate change treaties. Nor has it been accepted that this principle applies directly in the relations between States without having been specified in a treaty (see Case concerning the audit of accounts between the Netherlands and France in application of the Protocol of 25 September 1991 Additional to the Convention for the Protection of the Rhine from Pollution by Chlorides of 3 December 1976, Decision of 12 March 2004, United Nations, Reports of International Arbitral Awards, Vol. XXV, p. 312, paras. 102-103; see also ILC Principles on the allocation of loss in the case of transboundary harm arising out of hazardous activities, Yearbook of the International Law Commission, 2006, Vol. II, Part Two, pp. 74-75, paras. 11-15). Accordingly, the Court does not consider that the "polluter pays" principle is part of the applicable law for the purposes of this Advisory Opinion. This does not preclude the possibility that forms of strict liability for hazardous acts and other kinds of acts that are not wrongful under international law are developing.[977]

This paragraph is somewhat opaque. On the one hand, it seems to acknowledge that it is possible for direct obligations to be placed by international law on private actors—which is of course not news. Here it is the "polluter pays" principles under consideration; it may refer in some contexts to States (including responsibility for the sum total of private activity causing pollution in their jurisdiction) but the principle in Rio 16 is clearly meant to refer also if not primarily to non-state polluters. On the other hand, there is ambiguity as to whether the fact that States are expected to create legal frameworks to implement polluter pays means the ultimate duty in relation to private polluters having to pay is—as with due diligence—that of States and not a question of a direct international duty on private actors. That said, for this specific principle of polluter pays, the court is fixed on its very particular status and not on general questions of direct obligations of private actors under customary law. The court states its belief that the law (to date) requires a treaty to be the form in which the polluter pays principle becomes law—although, again, this is not a general statement about all norms that can be read as applying directly to private actors, but just this norm. Much is guarded and carefully crafted in this paragraph such as to leave open direct customary duties on private actors, while never actively entertaining or encouraging this possibility. Both of these sentences in the paragraph suggest that the non-treaty law of private obligations in the sustainable development realm (including future law on polluter pays) are left

[977] *Ibid* para 159-160.

open: “Nor has it been accepted that this principle applies *directly in the relations between States* without having been specified in a treaty” (emphasis added) and “This does not preclude the possibility that forms of strict liability for hazardous acts and other kinds of acts that are not wrongful under international law are *developing*” (emphasis added). “Developing” is a somewhat odd word to use for norms that may be on the horizon if one’s focus is on treaties versus on either custom or general principles—“being developed” would be the more obvious language to use. Considerable room seems to have been left for the kind of non-treaty instruments that involve hybrid actors (and thus not involving only the relations between States) and that produce practice beyond the text for recognition of the kind of transnationalized customary law discussed in this dissertation.

In light of these developments, I intend to pursue post-dissertation research examining the implications of this Advisory Opinion for ISDS tribunals. My inquiry will focus on how the Advisory Opinion may influence the resolution of investment disputes, particularly through a set of hypothetical questions: How may a host State invoke the law set out in the Advisory Opinion before an ISDS tribunal to justify its regulatory environmental measures (e.g, to what exact has a climate-change due diligence defence been created for the investment law sphere)? Could foreign investors be considered obliged to respect or protect the environment, either under the Opinion (e.g. due to the effect of States’ due diligence obligations on the legal characterization of the underlying private activity that attracts the need to for due diligence) or in spaces left open but not addressed by the Opinion (as discussed in the immediately preceding paragraph)? And what authority or status should both the Advisory Opinion itself as a juridical act and its comprehensive overview of the state of climate law be accorded in future investment treaty interpretation proceedings, given both the “advisory” nature of the judgment and the overall non-binding status of ICJ case law in a civil-law influenced understanding of public international law?

Such a post-dissertation study has the potential to reinforce my central objective of contributing to the realization of the *2030 Agenda for Sustainable Development* within the investment sector. By examining how Advisory Opinions in general and this one in particular may influence the intersection of investment law and environmental protection, the research will continue with the dissertation’s aspiration to foster a more balanced ISDS framework—one that upholds legitimate

regulatory space for environmental consideration while fostering the flow of foreign direct investments in line with global sustainable development goals.

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