

Integrating Investor Obligations and Corporate Accountability Provisions in Trade and Investment Agreements

REPORT OF THE EXPERT MEETING HELD IN
VERSOIX, SWITZERLAND, JANUARY 11-12, 2018

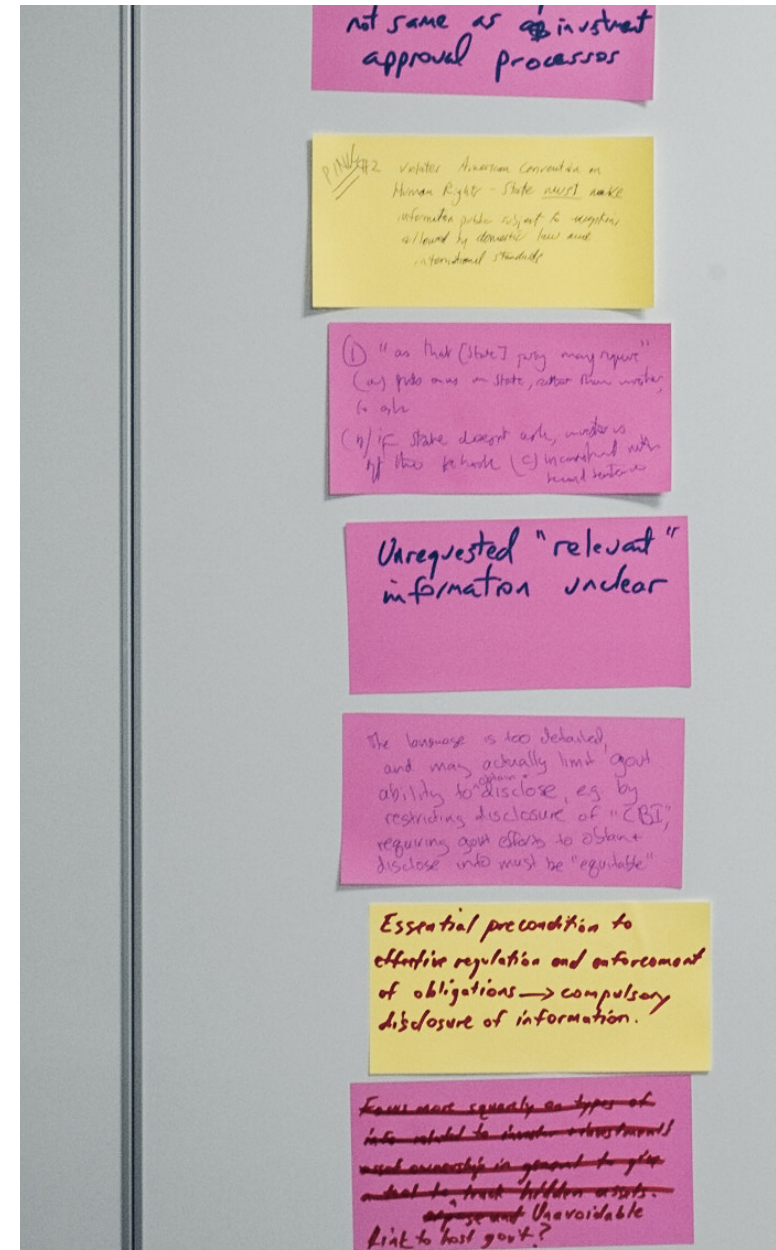
Co-hosted by the International Institute for Sustainable Development (IISD)
and the Friedrich Ebert Stiftung (FES)





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Introduction

On January 11 and 12, 2018, IISD and FES co-organized an expert meeting in Versoix, Switzerland, on the topic of Integrating Investor Obligations and Corporate Accountability Provisions in Trade and Investment Agreements. A diverse group of 30 experts assembled, with expertise ranging from diplomacy, economics, law and environment to the fields of investment, human rights and trade. Their discussion focused on finding a pathway to articulating and incorporating investor obligations in international economic agreements, specifically international investment agreements and international economic partnership or trade agreements with investment chapters.

The current international investment law regime has been the subject of much criticism. Topping the list is the asymmetry and imbalance between rights and obligations of foreign investors and host states. Many of the traditional investment treaties have endowed investors with broad rights and protections that are backed by strong dispute settlement mechanisms. States, on the other hand, have committed to non-reciprocal obligations that can significantly limit their policy space. For years, countries—particularly those from the global South—have been questioning the rationale behind this practice and have attempted to design models that strike a balance between investment

protection and legitimate policy space for public interest regulation.

It was noted at the beginning of the meeting that dozens of international standards, guidelines, principles, norms and best practices have been adopted to address the environmental, economic and social impacts of multinational enterprises. However, the impacts of these largely voluntary standards vary one from the other, and they do not always ensure that investment promotes sustainable development.¹ Moreover, it was noted that many of the communities and individuals who were negatively affected by investors' actions lacked effective access to justice—whether for prevention or remediation—under the international and domestic laws.² This was partly due to their lack of means to participate in the development of these laws. By contrast, international investment rules provide a mandatory framework for the protection of investment and international remedy for investors. The questions that would be examined at the meeting would be whether sustainable investment could be advanced by including it in international economic agreement provisions on

¹ See Daniel, C., Wilde-Ramsing, J., Genovese, K & Sandjojo, V. (2015). *Remedy remains rare: An analysis of 15 years of NCP cases and their contribution to improve access to remedy for victims of corporate misconduct*. Amsterdam: OECD Watch. Retrieved from https://www.oecdwatch.org/publications-en/Publication_4201. See also Daniel, C., Genovese, K., van Huijstee M. & Singh, S. (Eds.) (2016). *Glass half full? The state of accountability in development finance*. Amsterdam: SOMO. Retrieved from <https://www.grievancemechanisms.org/resources/brochures/glass-half-full>.

² UN Human Rights Council. (2017, July 18). *Report of the Working Group on the issue of human rights and transnational corporations and other business enterprises: Access to effective remedies under the Guiding Principles on Business and Human Rights: Implementing the United Nations Protect, Respect and Remedy Framework (A/72/162)*. Retrieved from http://ap.ohchr.org/documents/dpage_e.aspx?si=A/72/162.



investor conduct and how to strengthen remedies for stakeholders other than investors.

IISD prepared a background paper³ exploring various investor obligations that could be included in a trade or investment treaty. The background paper proposed a set of model provisions and commentaries inspired by and adapted from models and templates as well as bilateral investment treaties and trade agreements negotiated and adopted in Africa, Europe, India and Latin America. These provisions covered substantive obligations, access to compliance and grievance mechanisms, and potential civil liability resulting from the breach of the obligations. The participants to the meeting were invited to comment on these model provisions and share their views on: (1) the benefit of including them in a trade or investment treaty, (2) the flaws in the proposed draft provisions and (3) how the provisions can be further improved.

This report presents some of the main points that emerged from the discussions during those two days.



³ IISD. (2018). *Harnessing investment for sustainable development: Inclusion of investor obligations and corporate accountability provisions in trade and investment agreements*. <https://www.iisd.org/sites/default/files/meterial/harnessing-investment-sustainable-development.pdf>



General Obligation for Investors to Comply with Domestic Law

Background

Many investment treaties—including older ones—limit treaty protection to investments that have been made “in accordance with the laws and regulations” of the host state. In other words, the definition of investment determines the scope of treaty application. If the investment is not made in accordance with the applicable law of the host state, a tribunal would consider that there was no investment as defined in the treaty, making the treaty not applicable. Tribunals have approached this type of provision in different ways. Perhaps to make

applications of the provision more accessible, some recent treaties have also clarified the scope of dispute settlement, explicitly excluding protections for investments not made in compliance with domestic laws. Recognizing these recent developments, IISD’s texts additionally propose a standalone compliance article, which makes it clear that investors are expected to abide by the rules throughout the life cycle of an investment, not only when the investment is made.

Proposed Draft Texts

INVESTMENT

“investment” means, provided that the investment is established or acquired in accordance with the laws of the Host State and the obligations set out in this agreement.

SCOPE [OF ISDS]

For greater certainty, an Investor may not submit a claim under this agreement if the investment has been made or acquired in violation of domestic law or obligations set out in this agreement.

COMPLIANCE WITH DOMESTIC LAW

Investors and investments shall comply with all laws, regulations, administrative guidelines and policies of the Host State concerning the establishment, acquisition, management, operation and disposition of investments.

Discussions

Some participants considered this type of obligation too obvious to be included in a trade or investment treaty. Nevertheless, others pointed out a range of benefits for the inclusion of such provisions. For investors, these provisions could provide clarity and predictability in guiding their cross-border investment activities, especially in terms of the scope of treaty protection. For states, these provisions could stimulate thinking about the relationships between domestic and international laws and act as the basis for enforcing domestic laws using international mechanisms.



In terms of the content of the draft texts as proposed, participants noted that some of the language — for example “all laws, regulations, administrative guidelines and policies”—seemed to be over-inclusive, which may result in disproportionate consequences for minor violations. In this regard, it was suggested that there should be clear definitions and instructions for interpreting terms such as “laws,” “regulations” and “administrative guidelines,” etc. Some suggested the introduction of a standard of “material” violation. Others suggested that clarification should be provided in the determination of violations and proportionate consequences should result from different levels of violations.

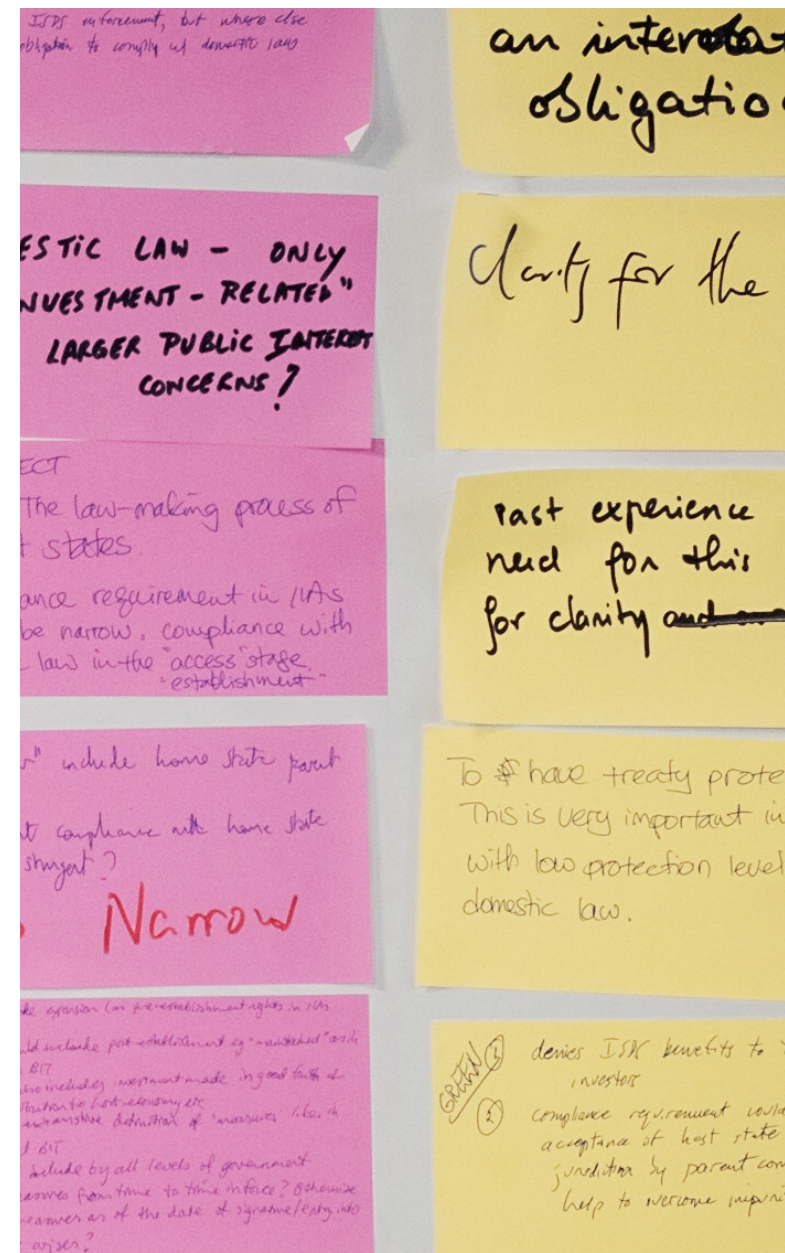
On the other hand, it was also noted that the proposed draft texts could be under-inclusive; for example, the texts failed to:

- Consider situations of bad-faith activities by investors that would otherwise be in compliance with the domestic laws and regulations.
- Consider situations where home state laws are more stringent than host state laws.
- Mention the obligation to comply with generally applicable bodies of international law such as international environmental law.

The draft texts as proposed also place the burden on the investors to be informed and to keep themselves up to date with relevant laws and regulations. In this regard, the draft texts should also include the corresponding obligation of states to ensure transparency of regulations or provision of information in accordance with their own laws. Furthermore, some participants cautioned that,

if liability is attached to a breach, excluding the investors from accessing investor–state dispute settlement (ISDS) proceedings would make the enforcement of the obligation difficult.

Participants generally agreed that a treaty should ensure that an investor complies with relevant domestic laws throughout the entire life cycle of an investment. To improve the proposed texts, participants suggested that the revision should take into account the competencies and responsibilities of different levels of government as well as the relationship between domestic and international jurisdictions. For example, mechanisms may be established so that investors’ breach of treaty obligation can be enforced at the domestic level. In this case, it is important to ensure that the domestic laws applicable to the investors are, at a minimum, consistent with international law in terms of promoting sustainable development. Where the domestic standards are lower than relevant international standards, those international standards should be expressly referenced in the treaty.





Anti-Corruption

Background

In recent years, an increasing number of investment treaties have explicitly included references to anti-corruption. IISD's proposed draft texts attempt to address both the demand side and supply side of the corruption equation by making it very clear on the face of the agreement that, if an investment is made through corruption, there is no access to ISDS. However, the proposed draft has no intention of replacing other possible enforcement approaches. For example, an investor who breaches the anti-corruption obligation may still face other domestic civil or criminal enforcement proceedings.

Proposed Draft Texts

1. *Investors and their investments shall not, prior to the establishment of an Investment or afterwards, offer, promise or give any undue pecuniary or other advantage, whether directly or through intermediaries, to a public official of the Host State, or a member of an official's family or business associate or other person in close proximity to an official, for that official or for a third party, in order that the official or third party act or refrain from acting in relation to the performance of official duties, in order to achieve any favour in relation to a proposed Investment or any licences, permits, contracts or other rights in relation to an Investment.*

2. *Investors and their investments shall not be complicit in any act described in paragraph 1, including incitement, aiding and abetting, and conspiracy to commit or authorization of such acts.*

Discussions

Recognizing corruption as a core problem of the current international investment reality, participants noted that the proposed texts dealt with one of the most obvious and fundamental obligations that should bind all investors. Although some doubted whether the law is the right vehicle to fight corruption, participants generally agreed that the inclusion of these provisions in a trade or investment treaty would uphold emerging international public policy, contribute to better and fair competition among investors, and send clear and correct messages to investors and host states on their anti-corruption obligations. It was further suggested that similar provisions should be drafted for fraud and intentional misrepresentation.

However, some participants pointed out that the draft texts as proposed represent a misalignment with relevant language adopted in the UN Convention against Corruption, which raised issues in terms of definitions of corruption, and thus could result in circumvention of the obligation. Broader and constructively vague language should be used to allow proper space for interpretation by enforcement agencies. Some suggested that a list of indicators or factors should be included to improve predictability of the application. Others suggested incorporating internationally accepted language from international conventions and other instruments (such as United Nations and Organisation for Economic Co-operation



and Development [OECD] conventions, and national laws like the Foreign Corrupt Practice Act of the United States [FCPA]).

Furthermore, there seemed to be a lack of clarification on issues relating to evidence and standard of proof to be applied in determining the breach. Some suggested that a civil law standard of proof should be applied if the breach is merely linked to the denial of treaty protection, while a criminal standard of proof should be applied if additional remedies are attached. In any event, participants suggested that the provisions should not be drafted in the form of strict liability; instead, fault should be proven for the finding of a breach, and there should be qualifiers such as “to the best of one’s knowledge.”

In terms of evidence, it was suggested that language should be included to allow disputing parties access to relevant documents and evidence. It was also suggested that the tribunal should be allowed to take any concurrent domestic proceedings into consideration, but that a finding by a domestic authority should not be required as a prerequisite to finding a breach of the treaty obligation. It was noted that language encouraging states’ cooperation in investigations should also be included. Noting corruptive conduct would, in many situations, involve actors other than the disputing parties, some suggested that there should be procedural safeguards ensuring the rights of non-disputing parties standing before the tribunal who might be accused of being involved in corruption.



Provision of Information

Background

The obligation of the investor to disclose necessary information to the government carries forward the anti-corruption idea to issues of fraud and misrepresentation in the making of an investment. The objective of the proposed texts is to encourage honesty and fair dealing. For this purpose, the provisions are drafted as a positive obligation with a specific reference not to provide fraudulent or misleading information. More specifically, the proposed language requires full and accurate information to be given to the host state government in order for it to be able to make

a decision whether to admit an investment or any other relevant decisions.

Proposed Draft Texts

1. *An Investor shall provide such information to a potential Host State Party as that Party may require concerning the investment in question and the corporate history and practices of the Investor, for purposes of decision making in relation to that investment or solely for statistical purposes. The Investor shall provide all other information relevant to the proposed investment decision, whether specifically requested or not, to the potential Host State making a decision in relation to*



admitting the investment. The Party shall protect any confidential business information from any disclosure that would prejudice the competitive position of the Investor or the Investment.

2. *Host States may make the information provided available to the public, including in the community where the investment may be located, subject to the protection of confidential business information and to other applicable domestic laws.*
3. *An Investor shall not commit fraud or provide false or misleading information provided in accordance with this Article.*
4. *Nothing in this Article shall be construed to prevent a State Party from otherwise obtaining or disclosing information in connection with the equitable and good faith application of its domestic law or in connection with disputes between the Investor and the State regarding the Investment.*

Discussions

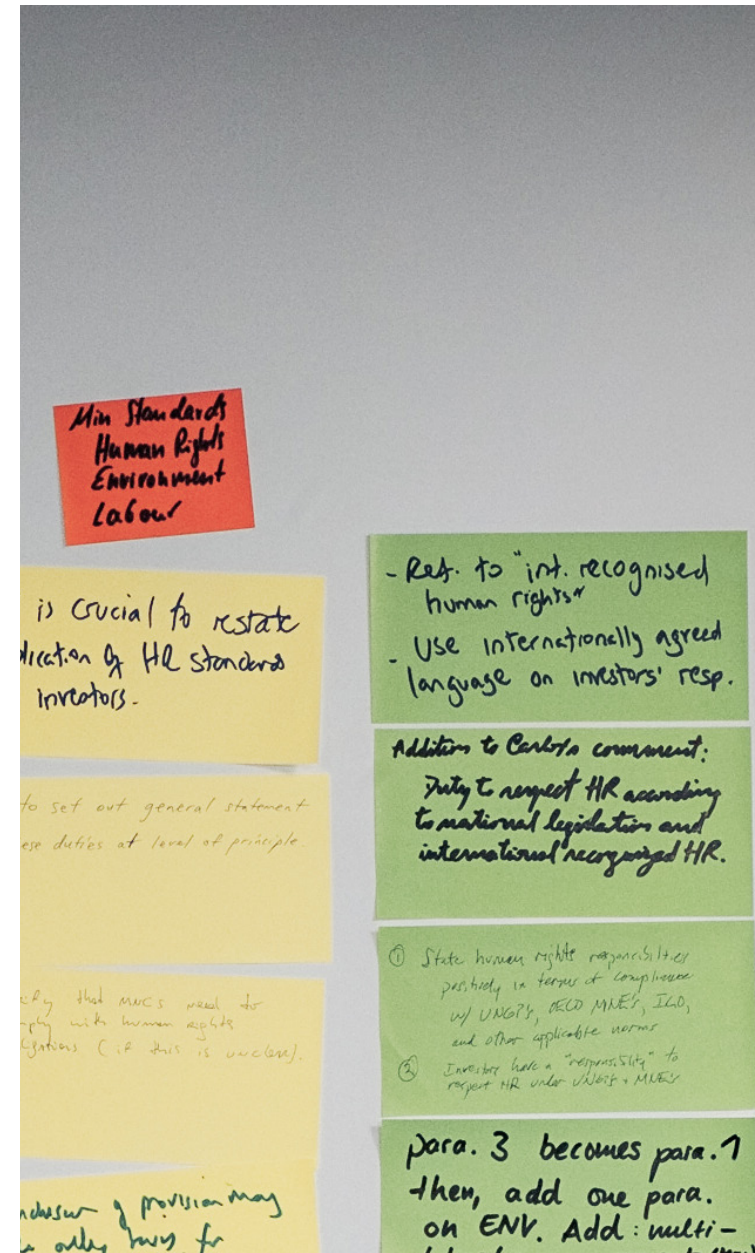
Although an obligation for investors to disclose information would allow the meaningful participation of communities in the decision-making process, some noted that the proposed draft texts allow the host state to use its discretion to determine whether to disclose information submitted by the investors. This seemed to be inconsistent with the ruling rendered by the Inter-American Court of Human Rights which held that, except for very rare situations, states have an obligation to make publicly available all information relating to their decision-making process.⁴ It was further pointed out that the

⁴ Claude Reyes et al. v. Chile, Merits, Reparations, and Costs, Judgment, Inter-Am. Ct. H.R. (ser. C) No. 151 (Sept. 19, 2006), para. 8-87.

proposed draft texts are vague on the institutional and administrative arrangement for submitting the information, and it was not clear whether the texts imposed an obligation on the host state to request and collect information or an obligation on the investor to provide information.

It was suggested that the term “relevant information” is too broad and should be properly defined; in addition, a list of information should be disclosed and the procedure for its disclosure should be specified in order to avoid potential abuse by states. Questions were raised about what would happen if there were conflicting rules under domestic laws regarding information disclosure. In this regard, some suggested the disclosure of global asset ownership and whether the investor faced any enforcement actions or had caused any adverse human rights impacts previously.

Participants also found a lack of balance between the need for confidentiality and the obligation to make the information public. It was suggested that reference should be made to domestic laws relating to the protection of confidential information and distinctions should be made depending on the different types of information to be disclosed.





Minimum Standards on Human Rights, Environment and Labour

Background

It is well demonstrated by various international instruments that corporations should behave in a way that is consistent with recognized environmental, labour and human rights standards and should not act in a manner that assists others in breaching such norms. However, until now, virtually all of the international treaty obligations on the environment, labour and human rights are imposed on states. By imposing a duty on investors and investments to respect internationally recognized environmental, labour and human

rights standards, the proposed draft texts seek to set a floor for conduct.

Proposed Draft Texts

1. *Investors and their investments have a duty to respect human rights in the workplace and in the community and State in which they are located. Investors and their investments shall not undertake or cause to be undertaken acts that breach such human rights. Investors and their investments shall not assist in, or be complicit in, the violation of the human rights by others in the Host State, including by public authorities or during civil strife.*

2. *Investors and their investments shall act in accordance with core labour standards as required by the ILO Declaration on Fundamental Principles and Rights of Work, 1998, as well as by the law in the Host State on labour standards.*
3. *Investors and their investments shall not establish, manage or operate investments in a manner inconsistent with international environmental, labour, and human rights obligations binding on the Host State or the Home State, whichever obligations are higher.*

Discussions

Participants recognized that the inclusion of this obligation would allow international obligations to be imposed directly on investors by clarifying investors' responsibilities not only for their own violations but also for violations that occur in the supply chain. However, many found the draft texts as currently proposed too restrictive and under-inclusive. It was noted that environmental obligations and labour standards deserve their own provisions.

Participants also noted that the term "human rights" should be further defined by using internationally agreed language,⁵ making reference to domestic legislation. In addition, well-accepted international standards such as the OECD Guidelines for Multinational Enterprises⁶ and the International Finance Corporation's Performance Standards on

⁵ Participants pointed to the UN Guiding Principles, which were unanimously endorsed by the United Nations Human Rights Council in 2011 (A/HRC/RES/17/4). United Nations. (2011). *Guiding principles on business and human rights*. Retrieved from http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf

⁶ OECD. (2011). *OECD guidelines for multinational enterprises*. Retrieved from <http://www.oecd.org/daf/inv/mne/48004323.pdf>



Environmental and Social Sustainability⁷ should also be included as the basis for these obligations.

In this regard, careful thought needs to go into which international environment, labour and human rights instruments are referred to and how. Participants questioned the rationale of limiting the obligations only “in the workplace and in the community and State in which they are located” (paragraph 1). It was suggested that better alternative language might be achieved by articulating the types of actors that multinational enterprises have responsibilities towards, and when those responsibilities should be engaged. It was further noted that additional guidance on the implementation of the provision is desirable. For example, mechanisms could be developed so that a tribunal could refer the matter to an independent third party or an independent expert body to guide the decisions of adjudicators.



Transparency of Contracts and Payments

Background

Developing countries widely use contracts to define the relationship between governments and private companies, particularly in the extractive industries sector. Unlike laws and regulations, the content of these contracts is typically unavailable to citizens, and they often contain confidentiality clauses. This has become a major issue. In recent years, several countries have recognized the benefits of making contracts public in certain sectors. The proposed draft texts intend to mainstream the practice so that it applies equally across sectors to all contracts and

payments made between foreign investors and host state governments.

Proposed Draft Texts

1. *[Unless explicitly prohibited by the laws of the Host State] Investors or their investments shall make public in a timely manner all contracts related to the establishment or right to operate an Investment made by the Investor or the Investment with a government in the Host State, subject to redaction of confidential business information.*

⁷ International Finance Corporation (IFC). (2012). *Performance standards on environmental and social sustainability*. Retrieved from https://www.ifc.org/wps/wcm/connect/115482804a0255db96fbfd1a5d13d27/PS_English_2012_Full-Documents.pdf?MOD=AJPERES



2. *Investors or their investments shall make public in a timely manner all payments made to a government related to the establishment or right to operate of an Investment, including taxes, royalties and similar payments.*
3. *Where feasible, such contracts and payments shall be made available on an Internet website freely accessible by the public..*

Discussions

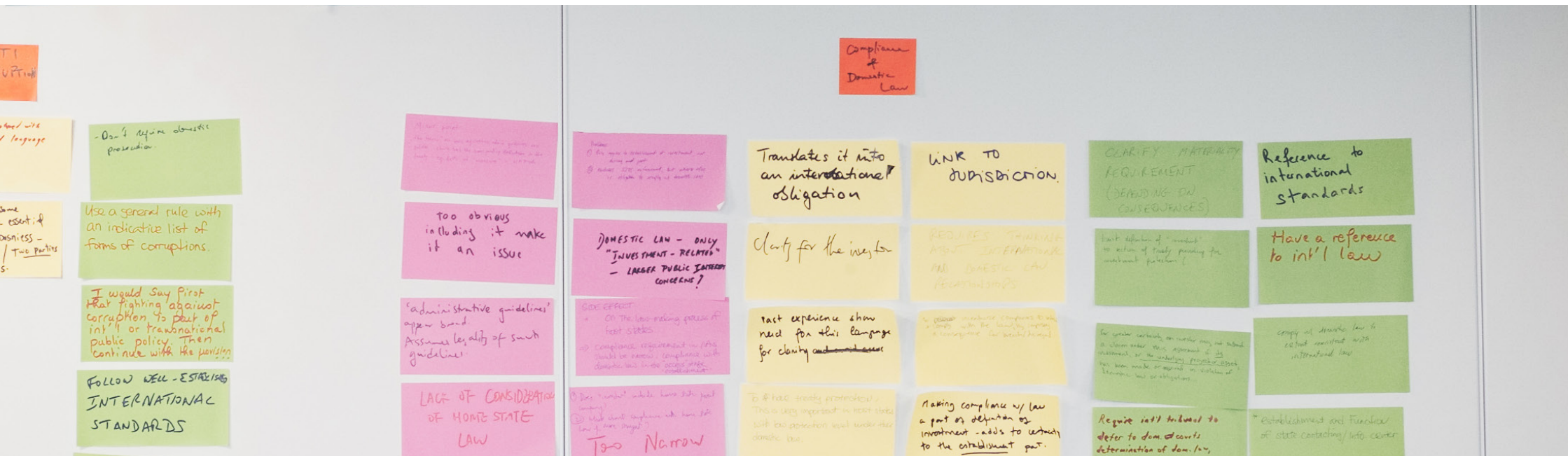
Participants noted that, as a general principle, all information involving public interest should be disclosed, as it is an important measure to safeguard the public interest and to prevent corruption. Acknowledging the approach taken by the Extractive

Industries Transparency Initiative,⁸ participants noted that similar measures should be adopted, but beyond the extractive sector. Participants also cautioned that ex-post contract and payment disclosure would not adequately cover payments made to entities other than the government, nor would the proposed draft texts cover private contracts with public interests such as security contracts, etc.

Some suggested that the obligation should be reframed as one that requires disclosure of project-related information rather than limiting disclosure to

concluded contracts or executed payments. Others suggested that affected communities should be provided with the right to request relevant information and that it should become an obligation for the investor to disclose such information when requested. Furthermore, it was noted that consent was an issue yet to be addressed, as, in many situations, consent by all interested parties involved in a project would be needed before certain information can be disclosed.

⁸ Extractive Industries Transparency Initiative (EITI). (2017). *Contract transparency (Guidance Note 7 – Requirement 2.4)*. Retrieved from <https://eiti.org/GN7>





Pre-Establishment Social and Environmental Impact Assessment

Background

As a critical part of the broader due diligence process, impact assessment has a great role in giving effect to states' and investors' duty to protect those affected by an investment; it also makes sound business sense. The language proposed by IISD aims to give effect to widely accepted requirements for impact assessments as an obligation on investors.

Proposed Draft Texts

1. *Investors or their investments shall carry out an impact assessment of their proposed investments prior to their establishment, as required by the laws of the Host State for such an investment [[or the laws of the Home State for such an investment] [or other performance standards], whichever is more rigorous in relation to the scale and nature of the investment in question].*
2. *Investors or their investments shall include in the impact assessment required under paragraph 1 assessment of the impacts on the human rights of*

the persons in the areas potentially impacted by the investment, including the progressive realization of human rights in those areas, or carry out a separate assessment on the same.

3. *The impact assessment or assessments shall be carried out by an entity that is wholly independent of the investor or its investment and any State with a stake in the investment.*
4. *The impact assessment or assessments shall include input from independent experts, such as international and domestic human rights lawyers, trade unions and environmental specialists.*
5. *The impact assessment or assessments must be carried out in a way that is transparent and accessible to the public, to investors and any other affected person. It shall in particular actively seek participation of the communities most likely to be affected by the investment and ensure that their input is reflected in the impact assessment.*
6. *Investors or their investments shall make the impact assessment or assessments:*
 - a. *public [including via the Internet] and;*
 - b. *accessible to the local communities, or other persons with potentially affected interests, in an effective and sufficiently timely manner so as to allow comments to be made to the Investor, investment and/or government prior to the completion of the Host State processes for establishing an Investment.*

Discussions

Participants recalled the well-established international consensus on investors' due diligence obligation throughout the entire life cycle of an investment. By carrying out proper impact assessments before, during



and after an investment, investors would economically benefit from being able to identify and address any problems early on. Also, proper impact assessment would benefit host states by ensuring the legitimacy of investment early on and presenting evidence for better policy-making. At the same time, impact assessment, when properly conducted, could also increase transparency and promote independent decision making by affected communities.

However, in order to ensure that an impact assessment can be properly carried out, several participants felt that IISD's proposed draft texts should provide further guidance in terms of: the content of and benchmark for impact assessment;⁹ the level of community engagement required; the relationship between impact assessment and other due diligence obligations; and the relationship between international standards and existing domestic mechanisms and requirements. For future revisions, it was suggested that the provision should be integrated as an element of the broader due diligence process, which should be inclusive, with meaningful participation by all stakeholders. A critical consideration for certain participants would be to ensure that the voices of affected communities are adequately represented during the process, either through the participation of community members or through the creation of a "public protector" role. Participants also discussed the importance of ensuring the proper design of the impact assessment

⁹ Reference was made to the Framework Principles on Human Rights and the Environment presented by the UN Special Rapporteur on Human Rights and Environment and welcomed by the UN Human Rights Council. J. N. Knox (2018). *Framework principles on human rights and the environment*. Retrieved from <http://www.ohchr.org/Documents/Issues/Environment/SREnvironment/FrameworkPrinciplesUserFriendlyVersion.pdf>

process so that it could effectively feed into the broader investment decision-making process. For example, recognizing the vital nature of the timing of the assessment process, participants noted that any assessment would need to be carried out within a timescale to allow it to influence decisions on granting investments in the first place.

Some participants also noted the lack of procedural safeguards ensuring the impartiality of the experts carrying out the impact assessments. For example, it was suggested that an independent body at the national level should be set up to carry out the required impact assessments. Some participants noted the importance of differentiating investments based on their nature, scale and sector, as it would be unrealistic to impose a single standard on all types of investments. It was suggested, for example, that a certain threshold could be developed to warrant a comprehensive impact assessment. Alternatively, a positive list of industries/sectors could be created, to which this obligation of conducting impact assessment would apply. Some participants also made reference to the practices of the IFC and Equator Principles, which categorize investments based on risks and only require impact assessments if the investments fall into the risky category.





Tax Base Erosion and Profit Shifting

Background

Recognizing foreign direct investment's direct contribution to the government revenue of a host state via corporate and business taxes, this section attempts to address two types of problematic corporate practices: tax base erosion and profit shifting (BEPS). Unlike tax evasion, which is illegal, BEPS practices are generally legal, which makes them complicated to regulate. The proposed text sets out five components to manage BEPS. The first concerns international financial accounting standards that investors should be required to adopt. The second introduces basic

arm's length principles for transfer pricing transactions between related companies. The third component is a general anti-tax avoidance clause, and the fourth reflects the related issue of transfer pricing in downstream transactions. The last element addresses the requirement for state parties to cooperate in areas of investigating and information sharing in relation to tax avoidance issues.

Proposed Draft Texts

1. *Investments shall meet or exceed national and internationally accepted standards of corporate financial governance for the sector involved, in particular for transparency and in the application of internationally accepted accounting standards.*
2. *Investors and their investments shall ensure that all transactions with related or affiliated companies shall be arms-length transactions at a fair market price. Investors and their investments shall not undertake any transfer pricing practices between themselves or any other related or affiliated companies.*
3. *Investors and their investments shall conduct their operations in a manner that fully complies with all applicable tax laws and international standards relating to ensuring tax benefits are not reduced through base erosion and profit shifting practices. Investors shall avoid undertaking aggressive tax or other financial practices which have such effects. Investors and their investments shall provide the financial information required by the host state to ensure compliance with the applicable laws.*
4. *Investors and their investments shall comply with all reasonable government requests for information on their supply chain and sales chain transactions.*
5. *States Parties shall cooperate in the detection and prevention of illicit financial flows and BEPS practices, including through the provision of information necessary to identify and prevent such acts.*



Discussions

Some participants shared their concerns about requiring investors to alter corporate practices that are perfectly legal under the domestic regime. It was suggested that imposing obligations on states to change their laws to prohibit such a practice might be a better way to achieve the same objective.

Some were also troubled by the phrase “aggressive tax or other financial practices which have such effects,” finding it too vague to enforce. If this type of provision is included in an investment treaty, it was suggested that the language should follow international instruments such as the OECD BEPS Actions as much as possible.

Furthermore, a number of participants questioned the use and effectiveness of the arm’s length principle. As an alternative, it was suggested that the provisions could be drafted to prevent investors from initiating dispute settlement proceedings in disputes involving changes to or adoption of tax measures.

In general, participants agreed that these corporate practices create impediments to sustainable development. However, some found that, in the context of an investment treaty, a more effective way to deal with the problem might be to address general sustainable development issues and focus more on disclosure-related tax obligations.



Relation to Investment Dispute Settlement

Background

Investor obligations in trade and investment treaties can be made effective and implemented in different ways. Some recent treaty and tribunal practices have barred investors from accessing ISDS if the investment is made through corruption or fraud, or is otherwise in violation of host state laws.¹⁰ However, this does not extend to the violations that may take place at a later stage of the investment. IISD’s proposed language

provides that, in case of violations occurring during the establishment of an investment within the context of a treaty that includes an ISDS mechanism, the investor loses his right to bring a claim. A similar approach could apply in the case of a state–state dispute settlement. As proposed by the draft texts, if the violation takes place at a later stage, a tribunal will hear the case but will have to take such violations into account when assessing the merits or damages. There may also be instances where investors’ behaviour is so grave that the tribunal will have to find their claims inadmissible. Given that the current ISDS mechanism does not allow states to initiate claims

¹⁰ See for example, Canada-EU Comprehensive Economic and Trade Agreement, Art. 8.18.3. Also see *Metal-Tech Ltd. v Republic of Uzbekistan*, ICSID Case No. ARB/10/3, Award, October 4, 2013.



against investors, the proposed language also provides for states to be able to initiate counterclaims against investors in ongoing proceedings.

Proposed Draft Texts

1. *Subject to any other specific directions under this Agreement as to the consequences of a breach of an obligation, where an Investor or its investment is alleged by a State Party in a dispute settlement proceeding under this Agreement to have failed to comply with its obligations under this Agreement, the tribunal hearing such a dispute shall consider whether this breach, if proven, is materially relevant to the issues before it, and if so, what mitigating or off-setting effects this may have on the merits of a claim or on any damages awarded in the event of such award.*
2. *Where the tribunal is of the view that the breach of obligation by the investor is fundamental to the nature of the claim, it may rule the claim inadmissible, or proceed only with the counterclaim by the State.*
3. *A Host State may initiate a counterclaim against the Investor before any tribunal established pursuant to this Agreement for damages or other relief resulting from an alleged breach of the Agreement.*

Discussions

Some participants saw the provisions as drafted as being a reasonable way to approach the consequence of violating investors' obligations within the existing ISDS arbitration framework. Many felt it was important to retain the opening phrase "Subject to any other specific directions under this Agreement..." as others—such as direct civil or criminal liability—should also be included as a means to enforce investor obligations.

In addition to "obligations under this Agreement" (para. 1), some suggested expanding the coverage of this section to other obligations committed to by the investors, such as those under domestic laws or contracts.

Questions were raised regarding the use of the word "inadmissible" (para. 2). Some participants expressed concern on the reviewability of a tribunal's decision on admissibility. It was noted that this would depend on whether there is intent to have the issue be reviewable. Thus, the provision should be drafted as a jurisdiction issue rather than an admissibility issue.

In terms of a counterclaim by a respondent state (para. 3), it was suggested that the provision should clarify that a counterclaim can relate to any issues

relating to the conduct of the claimant/investor, instead of being limited only to those issues already raised in the claim.

It was further suggested that, in addition to states' rights to counterclaim, the provision should also introduce a joinder procedure so that other interested parties can actively participate in the proceeding when needed.

The relationship of this section to domestic proceedings was also raised. It was suggested that relevant decisions and outcomes of domestic proceedings should also be taken into account by the tribunals.

As a procedural matter, it was noted that another issue that needs to be addressed is the qualifications and experience of adjudicators to determine the breach of a relevant investor obligation. It was further suggested that such a determination could be made by an independent institutional body or an ombudsperson as long as clear guidance on factors to consider is developed.



Tort and Civil Liability

Background

Given the significant challenges that many developing country host states face in seeking to regulate the activities of foreign investors, in many cases, communities and individuals adversely affected by a foreign investment would find it difficult—if not impossible—to achieve justice through domestic legal processes. One approach to overcome this situation is to allow affected communities and individuals to bring tort or civil liability claims in the courts of the investor's home state.

Proposed Draft Texts

1. *Investors and their investments shall be subject to civil actions for liability in the judicial process of their home state for the acts, decisions or omissions made in relation to the investment where such acts, decisions or omissions led to damage, personal injuries or loss of life in the host state.*
2. *Parties shall ensure that their legal systems and rules allow for, or do not prevent or unduly restrict, the bringing of court actions on their merits before domestic courts relating to the civil liability of the Investor for damages resulting from alleged acts, decisions or omissions of the Investor and/or its investment in the territory of other Parties.*

3. *In particular,*

- a. *each Party shall ensure that its domestic courts shall not decline to hear such actions based on forum non conveniens or any similar judicial rule in the Party.*
- b. *each Party shall allow its courts to look at the structure of the Investor and its investments to impose liability on the parent corporation and/or a sister subsidiary if the acts, decisions or omissions of the Investor or its investment led to damage, personal injuries or loss of life in the host state.*

Discussions

Participants shared their experiences in this regard and noted that various legal and procedural barriers exist today that prevent injured parties from accessing justice. Some of the salient points raised were:

- Forum non conveniens doctrine prevents the injured party from accessing home state courts.
- Complex corporate structures can prevent the injured party from reaching ultimate controlling shareholders.
- Parallel proceedings initiated by foreign investors have been known to frustrate the process initiated by injured party.
- It is a difficult challenge to collect or access evidence.
- The process can be costly and is not always efficient.
- The statute of limitations can bar the initiation of proceedings.
- Class action, a type of lawsuit where a group of people can be collectively represented in a proceeding, is not allowed in many jurisdictions.



- It can be hard for the injured party to have proper legal representation due to the complex and costly nature of the proceedings.

It was further noted that these issues have been recognized in the United Nations Guiding Principles on Business and Human Rights. The International Law Association's (ILA) *Report on International Civil Litigation for Human Rights Violations*¹¹ also proposed solutions to some of the challenges listed above, including various legal theories allowing claims to be initiated in a corporation's home state for human rights violations that had taken place in a host state. Some participants noted that many of the proposals in the ILA report are reflected in the Council of Europe Recommendation on Business and Human Rights adopted by the Committee of Ministers in 2016.¹²

In the context of these developments, participants identified two key concerns in addressing the existing challenges: establishing jurisdiction and establishing liability. In terms of establishing jurisdiction, participants noted the corporate veil issue caused by complex corporate structures. Some questioned the rationale whereby a shareholder can directly initiate legal proceedings to recover damages on behalf of its subsidiaries, but at the same time is protected by a corporate veil for any potential proceedings against its subsidiaries. On the other hand, participants

¹¹ International Law Association. (2012). *Final report: International civil litigation for human rights violations*. Retrieved from <https://ila.vettoreweb.com/Storage/Download.aspx?DbStorageId=1118&StorageFileGuid=59f7e403-7733-4f8c-822d-e58b9be0d02b>

¹² Council of Europe. (2016). *Human Rights and business: Recommendation CM/Rec(2016)3 of the Committee of Ministers to Member States*. Retrieved from <https://edoc.coe.int/en/fundamental-freedoms/7302-human-rights-and-business-recommendation-cmrec20163-of-the-committee-of-ministers-to-member-states.html>

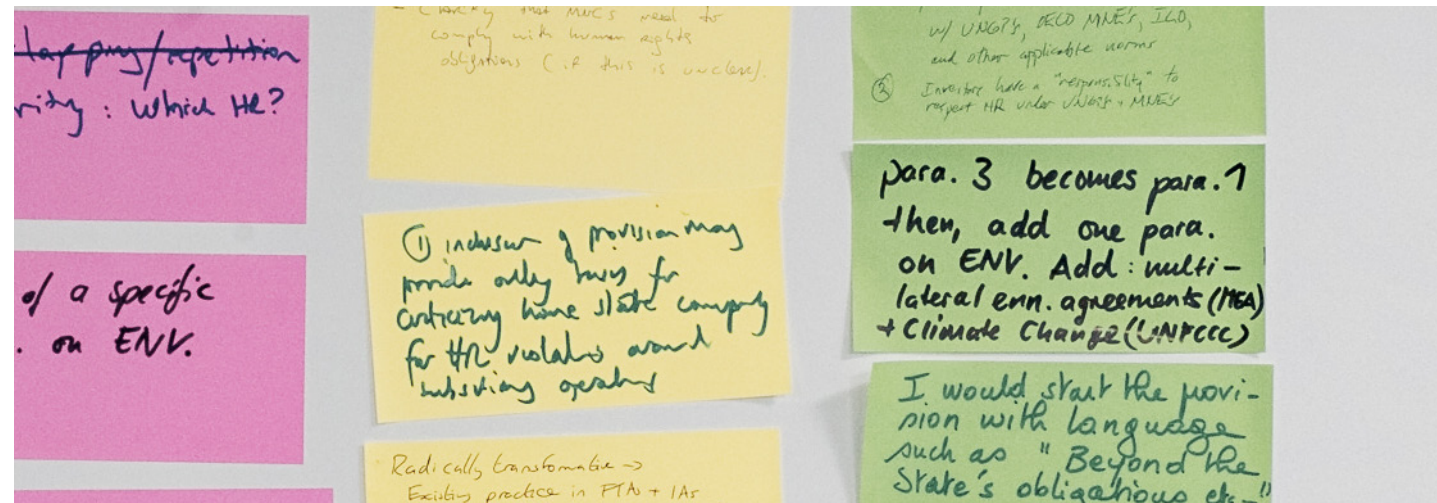
recognized that even if a claimant can successfully pierce the corporate veil, the jurisdiction would not cover those controlling companies operating under contractual arrangements, a situation commonly found in supply chains.

In terms of establishing liability, participants noted the importance of recognizing the principle of parent company duty of care and the principle on the duty of human rights due diligence. Access to information and evidence is also important. In this regard, it was suggested that there should be a reversal of the burden of proof in tort proceedings. For example, the human rights due diligence principle recognizes the duty owed by the investor, and it is up to the investor to produce evidence to prove that it has taken reasonable steps to comply with such duty.

Alternatively, it was suggested that in such proceedings the liability stage should be structured separately from the sanctions/damages stage. This

way, strict liability can be created for the violation of investors' obligations while still allowing investors to offer evidence to defend themselves and mitigate the sanctions with a shifted burden of proof. This is the approach taken by the United States Foreign Corrupt Practice Act.

In conclusion, participants found that, in addition to ensuring access to remedies for injuries that have already taken place, it is just as important to take steps to prevent violations. In cases of environmental or human rights violations, due to the serious nature of potential consequences, the importance of prevention should be further recognized. In this regard, it was suggested that, at the treaty level, one should prioritize the procedures that are most likely to enhance the reality of due diligence, either by providing more guidance or giving more incentive to corporations to invest the resources necessary for carrying out proper due diligence.





Other Issues of General Concern

Definition of Investor Obligations

Throughout the two-day meeting, the meaning of “investor obligations” was repeatedly brought up and debated by participants. It was noted that, in a broad sense, provisions laying out conditions relating to the behaviour of an investor could be seen as an investor obligation. Other participants suggested that, under a stricter view, “obligations” would have to be associated with remedies and enforcement against their non-compliance. Without this, these conditions could not be called “obligations.” Participants also noted the importance of determining whether even

small and inconsequential mistakes disqualify the investment. For example, in some cases, the breaches were a matter of international public order and could deprive the tribunals of jurisdiction, but in other cases, some tribunals might simply regard the breaches as trivial and part of doing business.

In this regard, it was noted that there could be different consequences for non-compliance with a particular obligation, depending on its nature.

- *Condition approach:* the enjoyment of a privilege is conditioned on compliance with certain obligations. For example, the investor may

be deprived of treaty protection if it is not in compliance with certain obligations.

- *Enforcement approach:* the breach of the obligation is directly enforced by procedures specified in the treaty or at the domestic level through the operation of the treaty.
- *Interpretation approach:* the fact of non-compliance will be taken into consideration when a tribunal interprets the treaty.

Definition of Investor

Participants also noted a need to clarify the definition of investor, to cover not only the project company but also the parent company, the ultimate controlling shareholder, as well as those along the supply chain. It is important to consider whether differential treatment should be given to certain investors depending on their nature, size or sector. It was also suggested that terms might have different meanings when used in different chapters of a trade or investment treaty. For example, the term “investor” in an investment protection chapter might be defined differently from the term used in a labour chapter.

Interpretation of Existing Treaty Language

In addition to elaborating new language to be included in a trade or investment treaty, some participants stressed the possibility of interpreting treaty language as a way of incorporating investor obligations into existing treaties. It was suggested that state parties could expressly make reference in the applicable law section of a treaty to investor obligations as reflected in internationally accepted



instruments or voluntary guidelines. It was argued that these instruments should, in any event, be taken into account by tribunals, as they reflect general international legal norms and transnational public policy. In addition, as an increasing number of transnational corporations have incorporated these instruments into their corporate policies, these should be taken into consideration when evaluating their behaviour. On the other hand, some participants cautioned against over-using soft-law instruments as a basis for enforcement, fearing that they could create potential negative consequences through disincentivizing investors from endorsing these instruments.

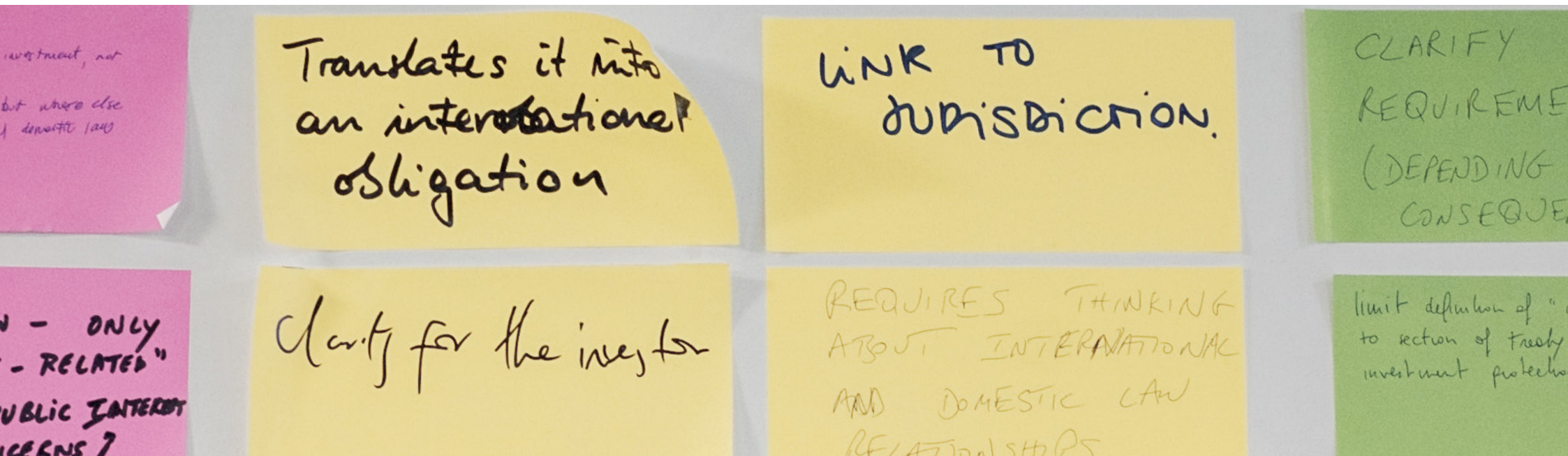
Other General Comments

Participants noted that investors' obligations may arise at any period during the entire life cycle of an investment, and this reality should be reflected in IISD's draft texts. Some expressed concern that the more detailed the language, the more it may provide room for circumvention. These participants expressed their preference for broad principle-based statements supplemented by a list of illustrative examples. On the other hand, some cautioned that broad terms, if not properly defined, may create vagueness and result in difficulty in implementation.

Participants also questioned the relationship between international law and domestic law in terms of their roles in regulating investor obligations. It is

important to articulate whether international norms set a minimum standard for domestic law and when the international regime can supplement what has been decided at the domestic level.

Lastly, it was noted that, since treaties are signed by countries with different political powers, political realities need to be recognized and considered at all times. When drafting a template document, it is important to take into consideration the trade-offs that will occur during negotiations, and that states, when using such templates, need to think about their respective negotiation bottom lines.





Conclusion and Ways Forward

Much common ground became apparent, as participants shared and debated their views during the two days of the meeting. Participants reiterated the concern that the current investment framework focuses primarily on investment protection. Accordingly, the existing ISDS mechanism only allows one group of actors—investors—to initiate claims against host states to enforce their rights. The only option currently available for a respondent host state to enforce investor obligations at the international level is by submitting counterclaims—though this is not always possible under current treaties either. It was generally agreed that it is important for treaties to ensure the effective use of counterclaims. Moreover, it was useful to explore what additional remedies the state should also have available at the international level in case of investor misconduct.

Participants also found that, under the current mechanisms, affected individuals and communities could not actively intervene in the proceedings initiated by investors and have to count on their governments to represent their interests and concerns. Several participants found that this was insufficient and that, at a minimum, interested parties should have the option to be brought into the proceeding through joinder. Participants also discussed the possibility of including a public protection system in adjudicative proceedings to represent the interests of non-disputing parties.

It was also recalled that direct international obligations for corporations have been tabled in

the context of the negotiations of an international binding treaty on business and human rights.¹³ The creation of an international tribunal has also been discussed in that context. In this respect, some participants suggested that, rather than establishing a new tribunal, a more effective way is to expand the jurisdictions of existing human rights tribunals so that they can deal with claims against corporations.

The role of national mechanisms (with some enhancement if needed) in the implementation of corporate responsibilities both in the host state and the home state was also discussed. Participants noted that, in addition to civil liability, it is also important to consider potential criminal liability for the violation of investors' obligations, and that, in this respect, international cooperation can play a particular role.

Participants generally agreed that if the discussions on the establishment of an international investment court were to bear fruit, it might make sense to include certain investor obligations in its jurisdiction. In any case, participants agreed that even if these were not explicitly addressed *ab initio*, the jurisdiction of such a court should not be designed so as to exclude future amendments in the scope of its jurisdiction.

Finally, despite the increasing number of trade and investment treaties and models concluded in recent

years incorporating investor obligations, participants noted that there still lacks a critical mass to pursue the reform of the substantive aspects of investor obligations. In terms of the ongoing processes, a number of participants believed that content and process should be discussed together.

Next Steps

IISD will conduct further research and revise the proposed draft texts, taking into account the views and comments expressed by the participants. IISD will also conduct further consultations on joint accountability and mediation processes—a topic that was included in the original background paper but that was not discussed at the Versoix meeting due to lack of time. IISD will prepare a set of revised draft provisions as a basis for future discussions and to provide input into ongoing negotiations at UNCITRAL, as well as at the bilateral and regional levels.

¹³ See the work of Open-ended Intergovernmental Working Group on Transnational Corporations and Other Business Enterprises with respect to Human Rights, available at <http://www.ohchr.org/EN/HRBodies/HRC/WGTransCorp/Pages/IGWGOntnc.aspx>



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