

Schriften zum Internationalen Recht

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Band 202

**Bilateral and Multilateral  
Investment Treaties and Their  
Relationship with Environmental  
Norms and Measures**

By

**Sonja Dünnwald**



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SONJA DÜNNWALD

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*Speak well of the law.  
Take care of your chest and voice, my good friend,  
and leave the law to take care of itself.*

Charles Dickens, *A Tale of Two Cities*



## Preface

This study was submitted for the degree of Doctor of Law at the Johann Wolfgang Goethe University Frankfurt (Germany) in January 2013. The text has been updated for this publication to reflect subsequent decisions of investment tribunals until June 2014.

I would like to express my sincere thanks to my supervisor Prof. Dr Dr Rainer Hofmann for his guidance and encouragement. I have greatly benefited from his advice and the freedom to approach the subject in the way I felt most rewarding. I would also like to thank Prof. Dr Isabel Feichtner, LL.M., for her rapid preparation of the second opinion.

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Frankfurt, July 2014

*Sonja Dinnwald*





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## Introduction

*The law locks up the man or woman  
Who steals the goose from off the common  
But leaves the greater villain loose  
Who steals the common from off the goose.*

Anonymous, 17th century

An investment in economic undertakings is likely to have political, social and environmental effects in addition to its economic results.<sup>1</sup> Economic activity regularly changes aspects of the natural environment and it risks having adverse effects: It depletes resources, causes pollution or consumes soil and water in fragile ecological systems. Significant economic projects are frequently driven by foreign investment, so that the desire to preserve the environment consequently has the potential to conflict with the obligation to protect foreign investment activity. Foreign entrepreneurs seek investment opportunities in any profitable business sector. The reasons for the decision to invest abroad are manifold. Particularly relevant motives are more favourable conditions to produce – such as lower wages and less regulation which is considered as ‘red tape’ – or a high demand for a particular service in the host state.<sup>2</sup>

Foreign direct investment can play an important role in providing financial resources to all sectors of the economy of the host state. One sector that often involves foreign investment is the exploration of natural resources, especially in developing countries, because those countries often do not have sufficient financial means and expertise for the exploration. The potential for tension is obvious with regard to such exploration: Activities such as deep-sea drilling for oil or mining invariably have an adverse impact on the natural environment and there is the inherent risk of significant destruction if things go wrong. The environmental implications resulting from

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<sup>1</sup> See the detailed portrayal of the development implications of investment, relying on the example of extractive industries, in *United Nations Conference on Trade and Development* (UNCTAD), ‘World Investment Report 2007, Transnational Corporations, Extractive Industries and Development’ (2007) pp. 130, 145–154. The Report is available at: [http://unctad.org/en/docs/wir2007\\_en.pdf](http://unctad.org/en/docs/wir2007_en.pdf).

<sup>2</sup> See, generally, *Giese, Alenka S. et al.*, ‘Foreign Direct Investment: Motivating Factors and Economic Impact’, 20 *Journal of Regional Analysis and Policy* 1990, 105–127.

excavation processes may differ, but consequences of the extraction of crude oil, coal, bauxite, or rare earth elements are well-documented and understood.<sup>3</sup>

Another sector frequently relying on foreign investment encompasses relevant infrastructure projects – such as the building of a highway, the construction and operation of a sewage system, or the engineering of power plants to provide electric energy. Investments linked to the construction and operation of a large energy generation plant or a hazardous waste facility are intertwined with environmental issues and they fuel the fear of environmental degradation. More generally, the occupation of territory by a factory in an area relevant for biological diversity and the emissions stemming from the productive process can be problematic.

At the same time, the international community and individuals around the globe increasingly become aware of environmental risks.<sup>4</sup> Consequently, some foreign investment projects are likely to raise genuine concern about their environmental impact. There will be legitimate opposition to projects, which stems from fear that an undertaking is not sustainable and will result in environmental degradation. It may take time to scientifically establish evidence on the environmental dangers of certain activities and substances, but the overall volume of recognised environmental dangers is ever-increasing. New scientific evidence and resulting international agreements to restrict detrimental activities often causes the host state to adopt new regulation, which can restrict the investment activity or induce additional costs for the alien investor.

However, host states may also have other reasons to restrict foreign investment activity. An economically profitable investment project is at risk of becoming the target of less legitimate economic desires. The host state may want to take over or participate in the project or may prefer its nationals, and not the foreign investor, to reap the profits. Accordingly, the state may want to assist and favour national competitors to the detriment of the foreign investor. To cover its protectionist intent, the host state may use environmental concerns as a smoke screen. Accordingly, referring to an alleged environmental purpose cannot be enough to consider a measure as legitimate. Investors in a foreign country are particularly vulnerable, because they have given up a substantial part of control, once capital has been invested and rooted in the host state. It is the task of international law to

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<sup>3</sup> UNCTAD, 'World Investment Report 2007, Transnational Corporations, Extractive Industries and Development' (2007) pp. 145–148.

<sup>4</sup> See portrayal in 'Chapter 1 – Environmental Norms and Principles', p. 30 *et seq.*

divorce legitimate from illegitimate regulation for both subject areas to exist in harmony.

The question whether international investment law exists in harmony with environmental norms and standards has been discussed for nearly two decades, most intensely in connection with the investment provisions of the 1994 North American Free Trade Agreement. The debate, which remains ongoing, is largely characterised by two opposing groups of scholars and practitioners:<sup>5</sup> One group, rooted in investment and trade law, argues that there is no risk of international investment law impeding legitimate environmental regulation. According to this group, respective concerns misrepresent the protective scope of investment law. The opposing group insists that the robust protection offered to foreign investment contravenes necessary efforts by host states to protect the environment. The perception is that investment protection is used as a sword by the investor against environmental protection to “wreak havoc on [...] environmental laws”<sup>6</sup>.

This study aims to evaluate the merit of the opposing positions by determining how investment decisions deal with environmental measures, norms and standards. Tensions between international investment law and environmental law will most certainly be dealt with in a forum of investment law – in the light of the ease with which individuals can trigger such proceedings. There are no comparable mechanisms in international environmental law, which lacks specified courts or similar institutions judging on individual claims.<sup>7</sup> In international state-to-state procedures outside the investment arena, environmental conflicts are generally confined to the role of a

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<sup>5</sup> There are no absolute, distinct categories of professionals working in this segment of law. However, it is more than accidental that the most active professionals appear to divide into either being pro liberalisation – thereby supporting strong investment protection – or being pro state – accordingly favouring the capacity of the state to regulate. In addition, the frequent affiliation of lawyers pro free trade and investment with international law firms has been commented upon.

In contrast, proponents of the role of the state in this context tend to have a background in the traditional areas of public international law and be less connected to major law firms. While there is a very recent trend towards reconciliation of both approaches and lawyers, the ‘world’ of academic commentary so far remains rather divided.

<sup>6</sup> In these terms, *Lindo*, Victoria R., ‘Hydroelectric Power Production in Costa Rica and the Threat of Environmental Disaster through CAFTA’, 29 *Boston College International and Comparative Law Review* 2006, 297 (309). Several commentators appear to share this view, but use less direct language.

<sup>7</sup> It appears as if individuals desiring an enforceable remedy relating to the protection of the environment deriving from an international treaty have to rely on a human rights approach. The most far-reaching instrument in terms of rights of the individual is the 1998 Aarhus Convention on Access to Information, Public Participation in Decision Making and Access to Justice in Environmental Matters. It is a