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BACKGROUND

Invoking investment treaties and investor–state contracts, transnational companies and other investors have been able to sue states challenging a wide range of measures, including public health and environmental measures, and measures involving projects with significant impact on local communities. With public policy issues at stake and with governments often condemned to pay multimillion dollar awards, public awareness and opposition to investor–state arbitration has increased significantly over the past few years.

In 2014, the International Institute for Sustainable Development (IISD) initiated a process with experts to discuss the simple question: “If investment-related dispute settlement mechanisms at the international level were to be built anew, what should they look like?” A consensus emerged among experts about the need to address the fact that people who are negatively affected or harmed by investment operations lack effective access to justice under international and domestic law, while foreign investors have access to international dispute settlement under treaties and contracts.

Building on the results of the 2014 meeting and recent developments in international practice regarding investment-related dispute settlement, IISD held a second expert meeting in May 2016. At the meeting, participants explored alternative models for settling investment-related disputes at the international level to supplement or replace existing mechanisms. There was a convergence of ideas from the participants at these two expert meetings that, in terms of process, a multilateral mechanism should not be limited to formal and binding adjudication but should also include so-called accountability mechanisms and multi-party mediation. It should be a mechanism where various parties could have access to justice, including states, affected communities and economic actors.

Given the extensive expertise of the Washington-based community, and in light of the current developments such as the European Union’s proposed Investment Court System (ICS) and new institutions like the Asian Infrastructure Investment Bank (AIIB) and the New Development Bank, on April 11, 2017, IISD and the American University Washington College of Law co-organized another expert meeting in Washington, D.C. The April 2017 meeting discussed ways forward on a compliance and dispute settlement mechanism on investment.

Building on the proposal advanced by David Hunter and Natalie Bridgeman Fields in their article published in 2008 to build a new foreign investor accountability mechanism, as well as the interim results of the multi-year process initiated by IISD, the purpose of the April 2017 meeting was to draw lessons from experience with the international accountability mechanisms (IAMs). These lessons would then inform the design of a new international mechanism for resolving investment-related conflicts and ensuring compliance with applicable principles and rules.

Investment-Related Dispute Settlement: Lessons from international accountability mechanisms

ISSUES

Participants generally agreed that there is a lack of meaningful remedies for communities in investment-related disputes. Some participants pointed to the problematic language repeatedly seen in existing and new trade and investment agreements as evidence of the lack of universal recognition of this issue.

One participant suggested that this was the result of some governments’ policy choice of prioritizing foreign investments over development. In this regard, some participants suggested breaking the issue into two parts: the procedural and substantive rights of the communities. Procedural rights refer to access to justice by means of a system or mechanism. As to this aspect, participants noted that there has been a visible trend across various institutions in recognizing the need of inclusiveness. However, there still are challenges in sufficiently demonstrating the empirical benefits of including communities as well as in providing the legal basis to include communities in the various proceedings.

Regarding substantive rights, participants recognized that this could be a more challenging issue to resolve, but that it could be partially addressed by allowing the meaningful participation of communities in the treaty negotiation process.

Another participant framed the discussion as a debate on (1) how to close accountability gaps and (2) how to make the investment-related dispute settlement system more just. To address the first prong of the debate, the participant noted that discussions should focus more on investors’ conduct and communities’ access to remedies. The second prong of the debate could be partially addressed by allowing communities to effectively participate in the proceedings.

ACTORS AND RELATIONSHIPS

COMMUNITIES

Currently in investment-related disputes, communities are typically not formal parties to the proceedings under investment treaties, but are nevertheless affected parties in many investment disputes. Participants noted some ongoing movements in different organizations to address community concerns, including new developments in the International Criminal Court to accept cases arising out of environmental harm and land grabbing.

Some also noted that the different interests between different community groups should not be ignored. For example, in the mining sector, some communities may be harmed by pollution, while others are employed by the company, gaining monetary and social benefits from the projects. Given the different interests involved, participants noted the importance of solution-oriented problem solving, for which mediation and other dispute resolution mechanisms may be more efficient than accountability mechanisms.

In other instances, participants suggested that communities may want to use an accountability process. It was noted that even if communities prefer alternative dispute resolution mechanisms such as mediation, incorporating a compliance element in the mechanism could help bring other actors to the table.

Participants recalled key challenges arising with respect to communities: How can community voices and concerns be heard and taken into account? What are the communities’ concerns and aspirations? How can a new mechanism respond to these concerns?

INVESTORS

It was noted that investors’ decisions whether or not to invest in a developing country could be influenced by low environmental and social standards and related lower costs. Participants agreed that, therefore, it is important to ensure that all investors are on a level playing field, to prevent a race to the bottom.

Participants also mentioned that investors are willing to pay for political risk insurance, showing that if a business opportunity offers enough prospects of profits for investors, they will invest. It was suggested that this risk-averse nature of investors could be used as leverage for their participation in an accountability mechanism. In this context, participants pointed to the Enhanced Corporate Social Responsibility Strategy issued by Canada in 2014. According to this strategy, as a penalty to Canadian businesses that do not embody corporate social responsibility (CSR)
best practices and refuse to participate in the dispute resolution processes listed in the strategy, the Government of Canada will withdraw support for those businesses in foreign markets. It was also noted that, pursuant to environmental and social standards of development finance institutions (DFIs), investors or developers also had to adhere to sound standards in order to access financing.

GOVERNMENTS

Some noted that, in practice, many investment-related disputes raised issues involving governments. Existing IAMs are weak on this point, causing various operational challenges, especially in the area of mediation. When conducting a mediation proceeding, it is more efficient when all parties—communities, investors and governments—participate in the process. In practice, however, even though the government agencies can be the entities actually implementing a project, they are rarely engaged in mediations conducted by the IAMs under the various international financial institutions. For disputes that start between communities and private investors, governments can also play a key role in resolving the issues and ensuring the continuity of the investment project. Participants indicated that these governmental concerns and interests could be used as leverage to bring the government into mediation processes.

Participants recognized the essential nature of having states’ buy-in to any proposed international mechanism. Some shared their concern that states would not want to see their domestic law be interpreted by a new international body or forum, and suggested housing the reform within an existing framework rather than creating a new one. Further, it was suggested that if the issue were to draw states’ attention to the new international mechanism as an alternative to existing dispute resolution mechanisms, enforceability would be a key issue on the table.

DEVELOPMENT FINANCE INSTITUTIONS

Participants noted that DFIs are often absent from investment-related disputes. Since DFIs do not directly implement activities or control enterprises that are subject to the type of regulation or rule that typically can lead to investment disputes, they rarely appear in any process. In most cases, DFIs only become involved in dispute resolution mechanisms when affected stakeholders complain to the DFIs’ accountability (compliance) mechanism about DFI-financed activities.

GENERAL PUBLIC

Participants recognized the importance of having buy-in from all stakeholders. Addressing the resistance from certain governments or lack of political will to address community concerns, some noted the recent wind of change in public sentiment. Noting the importance and high level of public buy-in for reform at present, one participant suggested referring to and drawing lessons from mechanisms adopted in various public approval processes, such as the passage of the environmental side agreement of the North American Free Trade Agreement (NAFTA) by the U.S. Congress, though opportunities for community engagement are limited here as well.

PROCESSES

DISPUTE PREVENTION AND DISPUTE RESOLUTION

Depending on the timing of the dispute in relation to the stage of the investment cycle, participants roughly distinguished between dispute prevention (including accountability and compliance mechanisms) and dispute resolution (both non-adjudicative and adjudicative processes). There is a key distinction between the two. The focus of a dispute prevention process is often on the investors’ activities, and the purpose is usually to ensure that the investment is carried out as planned by identifying and neutralizing the “hot-spots” that may result in future disputes if not properly addressed. In this case, as noted by some participants, the common interest of the various actors to continue the investment should be identified, so as to promote and leverage compliance.

In contrast, in dispute resolution cases, a dispute has already arisen. For example, as commonly seen in investor–state arbitration claims, a foreign investor upset by a measure adopted by the host state initiates the dispute resolution proceeding to challenge that particular measure. In these cases, it would be much more difficult to find shared interests among the disputing parties.
Some participants also noted the importance of enhancing processes prior to the dispute prevention stage to prevent the escalation of disputes. Referring to environmental impact assessment regulations issued by many countries in the late 1980s and 1990s, some participants noted the importance of access to information and rights to participation in the decision-making process. It is when these processes are not scrupulously followed that risks of community conflict most often arise.

INTERACTION BETWEEN VARIOUS PROCESSES

Participants recognized the importance of considering how different processes interact. For example, it was suggested that a treaty could create a mechanism to facilitate fact finding or mediation by leveraging investors’ preference for arbitration, by making investors’ good-faith participation in one of the mechanisms (for example, the accountability mechanism) a mandatory pre-condition of access to another mechanism (for example, arbitration). This could also be achieved through amendment of the existing treaties.

Others suggested an alternative formulation: if a mediation or facilitation fails, the injured party, including communities, could have access to otherwise unavailable mechanisms—for example, international arbitration. This could also be achieved through amendment of the existing treaties.

Participants asked whether it is efficient to address communities’ concerns in the same forum as other forms of dispute settlement or whether they should be addressed in parallel processes. Some noted further that it is not practical to engage in community-related debates in arbitration proceedings as most arbitrators are not competent in addressing environmental or social issues—or may not be motivated to do so. Therefore, community-related issues would have to be addressed, if possible in a judicial setting. It was also suggested that, in addition to a fact-finding function, an advisory function could be added to the dispute resolution process to compile or offer lessons coming out of the dispute resolution proceedings as an information basis for the adjudicators. The same participant also noted that, in many cases, no matter how dispute resolution processes are reformed, dispute prevention processes also have unique benefits, and noted that the only process that may have the tools to redress the harms inflicted on communities is the compliance mechanism. Other participants concurred that, although dispute resolution is valuable in some situations, a compliance mechanism can deter disputes due to the reputational consequences.

Therefore, it was noted that a “dispute resolution plus” mechanism should be developed, including not only dispute resolution mechanisms but also flexibility to access other dispute prevention processes. It was further noted that, despite the different ways to settle or deal with conflicts, community issues must be a part of the discussion no matter what process has been chosen.

LESSONS LEARNED FROM EXISTING PROCESSES

Participants discussed the difference in treatment between projects backed by DFIs on the one hand and projects funded only by private investors on the other. While the former provides communities with access to an accountability mechanism, private systems (such as Equator Principles financial institutions) do not. Moreover, it was noted that, in both cases, private investors had access to international arbitration (provided they are covered by an investment treaty). Participants agreed that where accountability mechanisms are available—contrary to the concerns expressed in the early days of the first IAMs—this did not result in a floodgate of claims, despite the relatively loose eligibility standards. Developments around a new mechanism would likely be similar.

The Operational Guidelines of the Compliance Advisor/Ombudsman (CAO) at the International Finance Corporation (IFC) were held as an example for conducting effective mediations. Among the various recommendations provided in the guidelines, participants focused on a few with proven success in practice: conflicts are best addressed at their root cause; rights to self-determination are essential; processes must be designed and managed strictly based on the
parties’ needs. However, it was noted that, before implementing these guidelines, a solid structure for the process needs to be in place, which would require capacity, access to information, and access to expertise and other building blocks that will provide the basis for an effective mediation process.

GENERAL PRINCIPLES
The participants identified general principles that should apply to both dispute settlement and accountability processes.

TRANSPARENCY
Some participants stressed that transparency should be a principle regardless of the type of process. Others noted that there could be a different transparency concern in community–private sector mediation or facilitation when compared with a process that involves governments or wider public interests.

INCLUSIVENESS
It was widely recognized among the participants that each of the processes must be inclusive and involve all stakeholders.

FAIRNESS AND EQUALITY
Noting that the inequality between different actors is contributing to the proliferation of investment-related disputes, participants agreed to the proposition put forth in the 2008 article by David Hunter and Natalie Bridgeman Fields that it is important “to give equal weight to the arguments of all sides before conducting an independent and impartial investigation.”

INDEPENDENCE
Aside from access to DFIs’ accountability mechanism, most communities can only hope to seek access through domestic courts. Even when they have access, given the lack of independence of courts in some countries, participants found that an independent look into the complaints brought by communities or individuals is the primary value-added element that can be brought by an international process.

They also noted that independence also needs to be assessed in light of how the operating costs of accountability mechanisms are dealt with. It was noted that the independence of a mechanism may not be fully guaranteed if it is entirely funded by governments. Similarly, an international mechanism involving the services of highly remunerated lawyers, possibly from large international law firms, who may have conflicts of interest would also cast serious doubt on its independence and impartiality.

Finally, some participants were of the view that, while an ad hoc mechanism might be most independent, this might not be practicable due to high operating costs, so that eventually the mechanism would have to be “housed” at an existing institution. Depending on the institution, this would result in more or less independence. It was noted that when the Inspection Panel of the World Bank was set up there was a discussion to create a separate institution. Due in part to cost considerations, however, it ended up as part of the World Bank, with various checks and balances to ensure an acceptable level of independence.

FINANCIAL ACCESSIBILITY
Some cautioned that the discussions on resources should be realistic. If communities are allowed to intervene or otherwise participate in a proceeding, they may be expected to pay a part of the cost. In addition, by participating in certain proceedings,
communities are subject to other parties’ discovery requests, which creates a significant additional financial burden for the communities. In this regard, participants noted the importance of improving local court systems and other domestic processes, and cautioned that allowing disputing parties to resolve their disputes under international proceedings would take away the incentive to improve local courts.

NORMATIVE FRAMEWORKS

Participants recognized the different normative frameworks usually applied to development finance projects as compared to privately financed investment projects. However, when communities are concerned, participants agreed that a single normative framework should apply to either situation. In terms of the possible norms to be included in such a framework, participants suggested that domestic laws should be a starting point and that other norms should be applicable, including relevant international law, community agreements, private contracts, soft-law norms (such as the Equator Principles for banks or any voluntary responsible business principles) and promises made by investors. Further, environmental impact assessment documents and conditions for permits can also be a part of the applicable norm, as those are also promises made by investors when making the investment. The applicable normative framework should represent an upward harmonization of principles, not the lowest common denominator.

Taking into account the above-stated point on upward harmonization, in terms of normative frameworks for compliance-based processes, participants questioned whether national laws and policies should be included in the normative framework and, if so, whether the laws of the host state or the home state should apply, as this question raises sovereignty issues. In either case, participants noted the importance of not allowing forum shopping to choose the lesser standard.

Some indicated that communities should use substantive standards such as IFC’s Environmental and Social Performance Standards in the beginning of negotiations to make their initial demands known and to strengthen their bargaining positions. The 2016 World Bank Environmental and Social Framework was also noted as a possible source.

CHALLENGES FOR DEVELOPING AN EFFECTIVE INTERNATIONAL ACCOUNTABILITY MECHANISM

SYSTEMIC CHALLENGES

Participants pointed to an important accountability gap resulting from the assumption that it should be entirely up to national law to address environmental and human rights concerns in the area of investment. While this assumption is justified to some extent, the reliance on national law and related processes is insufficient. In reality, individuals and communities generally lack access to effective remedies within national systems. Therefore, there is a need to fill the accountability gap with additional mechanisms. This gap has been filled to a certain degree where investment of DFIs are involved, where IAMs have been set up, but the number of projects covered is limited.

Even where IAMs are available, participants pointed to their limitations. In particular, they pointed to the lack of enforcement tools. Given that many investigations focus on the DFI itself, in some cases, the borrowers or the investigated companies may feel that the results of the investigation are not directly applicable to them and that they can ignore the results. It is then up to the DFI to pursue remedies that can reach the conduct of the borrowers. Participants questioned whether a new mechanism might help to address this problem. Some suggested that a newly established mechanism would also be more likely to deal with soft-law instruments, such as the Guidelines of the Organisation for Economic Co-operation and Development (OECD) or voluntary standards of industry associations. Like for existing mechanisms, it would be difficult to include a traditional enforcement role. Rather, it was noted, what is needed is a principal forum to engage in discussions where implementation and enforcement can be achieved through consensus-building exercises.

Outcomes of adjudicative dispute settlement processes also create some challenges. Participants noted that some of these dispute settlement processes typically lead to monetary damages, but do not award title of land or
determine that a law or regulation be amended or repealed.

Another systemic challenge lies in the communities’ limited access to mechanisms and knowledge. As noted by some, communities often do not even know that a particular mechanism exists, while other times communities are threatened by governments or investors if they use the mechanism. Further, communities often lack basic information about the project that would be needed for them to access relevant mechanisms.

OPERATIONAL CHALLENGES

Participants noted another major accountability gap in the prevailing IAM compliance process. For example, after a compliance report is issued, an action plan is usually prepared. However, in current practice, a number of action plans were prepared without engaging the community that brought the complaint in the first place.

It was stated that some “highly politicized” management teams of DFIs have made the processes essentially self-monitoring, which has significantly affected the credibility of mechanisms. In addition, it was noted by some, but not shared by others, that allowing general counsels of the investor or financier to play an important role in compliance and accountability processes creates significant conflict-of-interest challenges.

AREAS OF REFORM FOR ENHANCING THE EXISTING INTERNATIONAL ACCOUNTABILITY MECHANISMS

Participants brainstormed on the reforms they would like to see with respect to existing IAMs. While not representing consensus, suggestions proposed for incorporation in the new IAM to be developed included the following:

• Developing reporting on the implementation results of the accountability process.
• Introducing stronger sanctions to ensure compliance with the results of the accountability process, for example, by linking compliance to judicial mechanisms.
• Establishing a link between compliance and the benefits available from the home state.
• Introducing the possibility to stop a project under specific grave circumstances as one of the remedies.
• Involving civil society organizations and other actors to promote and monitor the effective implementation of the outcomes of the process.
• Ensuring more independent panels by redesigning the selection and qualification process.
• Enhancing capacity building at the community level to increase awareness of the available mechanisms.

• Securing adequate funding to help injured communities to access the mechanisms.
• Avoiding the proliferation of mechanisms that would lead to a lack of consistency and predictability.
• Exploring the use of insurance schemes or escrow funds as supplemental means for providing justice to the affected.

NEXT STEPS

1. Influence ongoing international efforts to create an investment court to include an accountability and mediation function

The discussions in Washington D.C. have solidified the view that creating a new accountability mechanism could be useful. If agreed to at the multilateral or the regional level, a new mechanism could serve to avoid the proliferation of new standard- or institution-specific mechanisms. A new mechanism could build on the lessons learned from existing IAMs and would fill the gap of soft-law principles and standards that currently lack effective implementation and compliance mechanisms.

With the European Union leading efforts and discussions around the establishment of a permanent Multilateral Investment Court (MIC) and similar efforts at the United Nations Commission on International Trade Law (UNCITRAL), there is currently an unprecedented opportunity to move forward the idea of improving access to remedies through the creation of a new accountability and mediation function.
Both the EU MIC proposal and the report prepared by the Geneva Center for International Dispute Settlement (CIDS) for the discussions at UNCITRAL take a narrow approach to reform: replacing investor–state arbitration with a more permanent form of investor–state dispute settlement.

This narrow approach does not address investment-related dispute settlement in a holistic way, as it would be limited to receiving claims brought by investors under investment treaties. Even if it were extended to cover investor–state contracts, as does the International Centre for Settlement of Investment Disputes (ICSID), the coverage of the new multilateral “court” would remain narrow in terms of potential substantive coverage (investment protection provisions), stakeholders (investors versus states) and methods (primarily formal and binding dispute settlement).

This debate should be broadened to ensure more inclusive forms of binding dispute settlement and include fact-finding, accountability and mediation. Building on the experience of IAMs, a new multilateral mechanism should allow for innovative solution-oriented dispute prevention and resolution through fact-finding and mediation. The accountability mechanism would be particularly useful with respect to investment-related soft-law rules and voluntary standards, such as the OECD Guidelines for Multinational Enterprises or the Equator Principles. States or other actors, such as Equator Principles financial institutions and companies receiving funding from those institutions, could opt in to such a mechanism.

The structure and institutional home would have to be tailored to the overall objective of the mechanism. It could be based in one or several existing institutions or secretariats or be newly created. It could have tenured judges and mediators or panellists or use a roster system. Different funding models would have to be explored in light of different types of complaints, disputes and stakeholders.

Building on previous research and expert consultations, IISD will further define and draft a convention to create a new comprehensive and inclusive investment-related dispute settlement mechanism. This mechanism will include accountability and multi-party mediation functions. The work will be channelled into the processes initiated in the European Union and the United Nations, as well as at the regional level, where the opportunity arises.

2. Propose and advocate the inclusion of an accountability and mediation function in trade and investment agreements

As the European Union and several countries are beginning to rethink their approaches to investment treaties, an opportunity arises to propose new ways forward. Discussions are already taking place in the European and EU member state parliaments about balancing investor rights and obligations in investment treaties and chapters, and integrating sustainable development objectives into trade and investment agreements. The European Union, for example, began including sustainable development chapters in its trade and investment agreements, starting in 2011 in its agreement with South Korea. Since then, these chapters have become a standard part of EU trade and investment agreements, and are now also included in agreements with investment protection chapters, such as those with Canada, Singapore and Vietnam. The chapters include provisions on international labour and environment standards and agreements, and also contain provisions on CSR, encouraging state parties to apply them. However, the provisions are all carved out from the treaty’s dispute settlement mechanism, and are instead subject to a special mechanism based on state–state consultations only.

Against this background, the time is ripe to propose the integration of new accountability and mediation mechanisms in new trade and investment agreements to ensure responsible business conduct in cross-border investment. For example, states could commit to setting up an accountability mechanism to ensure compliance with the guidelines and standards as accepted by the state parties for multinational enterprises, such as the OECD Guidelines. It would help tackle labour and human rights issues in global supply chains and put some responsibilities onto transnational corporations where implementation and compliance monitoring through the host state is weak. A new provision could set up a roster of professional mediators and panellists that would investigate compliance with these
guidelines and standards. This process would be additional to, alternative to or in replacement of existing mechanisms, such as the OECD national contact points. The OECD Secretariat or another mechanism (such as one of the existing IAMs) or a new mechanism (set up by the treaty parties or by an existing body) could serve as secretariat to receive complaints by affected individuals or groups.

Building on the expert discussions in Washington D.C. and further consultations and research, IISD will develop draft provisions to incorporate accountability and multi-party mediation mechanisms in trade and investment agreements. These would form part of a broader package for balancing investor rights and obligations and for reforming investment-related dispute settlement.

3. **Propose options for rebalancing rights and obligations in investment treaties and chapters through the incorporation of obligations and liabilities for investors**

In addition to the accountability mechanisms above and building on model templates and agreements, IISD will develop options on how to promote responsible investor behaviour through meaningful obligations and associated processes in trade and investment agreements. Integrating investor obligations in trade and investment agreements is a necessary step towards achieving a better balance between different stakeholders. We will build on templates and agreements already developed by countries such as Egypt, India, Morocco, Nigeria and others, as well as in regional groupings such as the Common Market for Eastern and Southern Africa (COMESA), the Eastern African Community (EAC), the Southern African Development Community (SADC), and at the pan-African level. The options will complement developments in the United Nations on business and human rights. We will also propose ways how to link these obligations and processes to any multilateral dispute settlement mechanisms that might be developed in the future.