

INTERNATIONAL INVESTMENT AGREEMENTS & SUSTAINABLE DEVELOPMENT:

SAFEGUARDING POLICY SPACE & MOBILIZING INVESTMENT FOR A GREEN ECONOMY

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ACRONYMS

BITs	Bilateral Investments Treaties
CBD	Convention for Biological Diversity
FDI	Foreign Direct Investment
FTAs	Free Trade Agreements
GCF	Green Climate Fund
GEF	Global Environmental Facility
GVC	Global Value Chain
ICSID	International Centre for Settlement of Investment Disputes
ICTSD	International Centre for Trade and Sustainable Development
IAs	International Investment Agreements
IISD	International Institute for Sustainable Development
ILO	International Labour Organization
IPAs	Investment Promotion Agencies
IPFSD	Investment Policy Framework for Sustainable Development
ISDS	Investor-State Dispute Settlement
MEAs	Multilateral Environmental Agreements
MFN	Most-Favoured-Nation
MIGA	World Bank Group's Multilateral Investment Guarantee Agency
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
PAGE	Partnership for Action on Green Economy
PPPs	Public-Private-Partnerships
SCC	Stockholm Chamber of Commerce
SDGs	Sustainable Development Goals
UNCTAD	UN Conference on Trade and Development
WEF	World Economic Forum

I. INTRODUCTION

International Investment Agreements (**IAs**) are treaties between States to promote and protect foreign investment under international law. By concluding IAs, capital-exporting countries (home States) aim to offer an additional layer of protection to their domestic companies investing abroad, while capital importing countries (host States) aim to attract additional foreign investment to their economy. Over 2,500 IAs are currently in force, mostly in the form of Bilateral Investments Treaties (**BITs**) or as investment chapters in broader commercial agreements that address trade as well as other matters (Free Trade Agreements, or **FTAs**).¹

IAs can play a useful role in mobilizing and channelling the investment needed for countries to transition to inclusive green economy pathways. The UN Conference on Trade and Development (**UNCTAD**) estimates that between US\$ 5-7 trillion worth of investment a year is needed to realize the Sustainable Development Goals (**SDGs**) adopted in 2015, including those necessary for infrastructure, clean energy, water and sanitation, and agriculture.² Yet, too much investment is still taking place in high-carbon and resource-intensive polluting sectors, placing additional burdens on the environment. By creating the appropriate incentives, IAs have the potential to facilitate investments that contribute to sustainable development and that support a country's transition towards an inclusive green economy that improve human well-being and social-equity, while significantly reducing environmental risks and ecological footprint.

However, the way many IIAs are designed at present overlook the importance of environmental and social considerations. Moreover, in their present form and operation, IIAs may restrict the ability of States to implement enabling policies for inclusive green economy pathways, particularly in the energy, transportation, agricultural, industrial, water, and waste sectors.

Typically, IIAs – whether in the form of BITs or as chapters in FTAs – have three main components:

1. Definitions of what constitute an ‘investment’, a ‘foreign’ investor, and the scope of protection offered by the treaty;
2. Several standards of investment protection (e.g. protection against expropriation, fair and equitable treatment standards, non-discrimination standards, etc.); and
3. A dispute settlement mechanism, often providing foreign investors the possibility to bring claims against the host State before an international private tribunal (arbitration tribunal) formed for each specific dispute for violation of one or more standards of investment protection.³

Investment disputes, as the claims brought before arbitration tribunals are called, have become very frequent since the 1990s, with dozens brought every year against countries all around the world. In a significant share of the overall amount of investment disputes, IIAs have been used to bring claims, sometimes for very substantial amounts (hundreds of millions or even billions of US dollars), against host countries in cases with environmental components (e.g. concerning energy production, waste treatment, water distribution, mining, etc.).⁴

Legal commentators⁵ and, increasingly, international organizations and governments, have warned about the risks to sustainable development that may arise from IIAs. However, while the complex interaction between IIAs, sustainability and inclusive green economy pathways has been discussed for some years now, this has, so far, mostly taken place in specialized circles. In order to comprehensively address the risks that may arise from IIAs and to realize the potential of IIAs to support a country’s transition towards an inclusive green economy pathway, stakeholders in the environmental policy and development sectors need to be actively engaged and involved in the negotiation of IIAs and the implementation of processes to reform existing IIAs. This includes, in particular, representatives of ministries for environment, development and social policy, as well as national planning commissions and other relevant government bodies that are charged with implementing international agreements, including the 2030 Agenda,⁶ the Paris Agreement on Climate Change the Convention for Biological Diversity (CBD), and many other multilateral environmental agreements (MEAs). Furthermore, those designing, interpreting and implementing IIAs need to do so in line with the mandate provided by the 2030 Agenda; to employ

trade and investment as vehicles for sustainable development, and refrain from subordinating environmental protection and social concerns to investment protection and an unbridled quest for growth at all costs.

In response to discussions that have taken place thus far, a still small but growing share of the entire body of IIAs, particularly the most recent agreements,⁷ have started to take into account environmental, social and labour issues in their text and structure. This has been done, for example, by inserting clauses stating that countries should not seek to attract foreign investment by lowering their environmental and social protection standards or by stating that the powers of countries to regulate for the common good are reserved. This is an encouraging trend towards a reconceptualization of IIAs based on the understanding that, like trade, foreign investment is not a goal in itself but an instrument to promote sustainable development.⁸

In this overall context, the purpose of this document is three-fold. Firstly, it is intended to raise awareness about the potential risks that may arise from IIAs that are not adequately designed and implemented, as they may restrict a country's ability to protect its environment and implement enabling policies for inclusive green economy pathways. Secondly, it aims to demonstrate the potential of IIAs to support the transition to inclusive green economy pathways and sustainable development. Thirdly, based upon these elements, it provides recommendations on the main avenues that can be explored to make IIAs a more suitable instrument for sustainable development. This document is targeted to a wide audience of government officials, political decision-makers, members of civil society, and the private sector. It focuses on environmental sustainability, while also taking into account the social and economic considerations of a country's transition to inclusive green economy pathways.

The document is structured as follows. Firstly, it provides a summary of international policy processes that seek to align IIAs with environmental protection, sustainable development and, more generally, with the mandate of the 2030 Agenda ([section II](#)). It then reviews both the opportunities and the potential risks for a country that may arise from entering into IIAs ([section III](#)). In the final section ([section IV](#)), the document takes stock of the main lessons learnt and provides recommendations on how to address the risks and maximize the potential of IIAs to become a vehicle for sustainable development and for transitioning to inclusive green economy pathways, as mandated by the 2030 Agenda.

II. THE LINK BETWEEN INVESTMENT AND SUSTAINABLE DEVELOPMENT

THE 2030 AGENDA AND THE [SDGs](#)

The 2030 Agenda, adopted by Heads of State in 2015, recognizes the importance of mobilizing adequate financial flows in order to realize the [SDGs](#). In particular, the 2030 Agenda recognizes the importance of private finance 'leveraged' by international public funds.⁹ Leveraging can be understood as a process by which international public funds (e.g. from a multilateral agency or a development bank) are allocated to a project or an initiative in order to reduce the risk for the private sector to either invest funds or lend funds to the project promoters. This is the main approach that has been pursued so far by environmental funds, such as the Global Environmental Facility (GEF) or the Green Climate Fund (GCF), in their efforts to engage with the private sector in order to help mobilize the investment required for mitigating climate change and enhancing environmental sustainability.

The 2030 Agenda also sets concrete goals and targets in [SDG 17](#) as well as in a number of substantive [SDGs](#). Trade and investment are seen as means for promoting sustainable development in [SDG](#) targets 2.a, 7.a and 10.b, which relate to food security, energy and inequality among countries.¹⁰ [SDG 17](#) refers more generally to finance, technology transfer, capacity-building, trade and a number of systemic issues (policy and institutional coherence, multi-stakeholder partnerships, as well as data, monitoring and accountability) as a means

to ‘revitalize the global partnership for sustainable development’. Although investment is not singled out, it is implicit in these references, not only with respect to finance and technology transfer but also to trade, which is a key component of many IIAs (in the case of FTAs).

Indeed, SDG targets 17.3 and 17.5 emphasize the need to mobilize resources from a variety of sources for developing countries, particularly least developed countries. It is also worth noting the explicit reference in SDG target 17.15 to the need to ‘[respect] each country’s policy space and leadership to establish and implement policies for poverty eradication and sustainable development’. This reference partly resulted from the debate over the so-called ‘regulatory chill’, – the constraints that may be imposed by trade and investment liberalization agreements on countries’ ability to adopt regulatory measures – including for environmental and social protection. As such, the 2030 Agenda clearly recognizes trade and investment as a means for achieving sustainable development that must be aligned with sustainable development objectives and a country’s legitimate regulatory function.

Finally, the 2030 Agenda expressly refers to the *Addis Ababa Action Agenda*,¹¹ adopted at the Third International Conference on Financing for Development earlier in 2015, as an integral part of the 2030 Agenda for Sustainable Development. The Addis Ababa Action Agenda specifically links investment to sustainable development. For example, it invites the private sector ‘to invest in areas critical to sustainable development’¹² and recognizes ‘the important contribution that direct investment, including foreign direct investment, can make to sustainable development, particularly when projects are aligned with national and regional sustainable development strategies’.¹³ Moreover, it describes a number of steps that could be taken at the national (e.g. by national investment promotion agencies) and international levels (e.g. through the World Bank Group’s Multilateral Investment Guarantee Agency or **MIGA**).

Importantly, the Addis Ababa Agenda emphasizes the need to safeguard the ability of States to regulate in pursuance of sustainable development. It affirms that ‘[we] will respect each country’s policy space and leadership to implement policies for poverty eradication and sustainable development, while remaining consistent with relevant international rules and commitments’.¹⁴ Later, it specifically refers to the need to regulate in order to align private investment and public goals: ‘[we] will develop policies and, where appropriate, strengthen regulatory frameworks to better align private sector incentives with public goals, including incentivizing the private sector to adopt sustainable practices, and foster long-term quality investment’.¹⁵

The goals set by the 2030 Agenda and the needs expressed in the Addis Ababa Action Agenda could be pursued through a number of ongoing international initiatives that focus on action at the domestic and/or the international level. The scope and objectives of these initiatives are not necessarily aligned; some focus

on investment ‘facilitation’ without a clear environmental objective, some others on social development and, still some others more specifically on environmental protection. The discussion that follows is intended to raise awareness of some significant processes which could potentially be used to redirect investment from the brown economy to low-carbon and green sectors.

INVESTMENT FACILITATION

A discussion relating to investment facilitation for development has been ongoing in some circles, including – informally – in the World Trade Organization as well as in E15, a non-governmental initiative co-organized by the World Economic Forum (WEF) and the International Centre for Trade and Sustainable Development (ICTSD). Two important limitations of these processes must be noted. Firstly, they expressly refrain from discussing matters relating to market access, IIAs and Investor-State Dispute Settlement (ISDS), which were considered too controversial to be included in the discussions. Secondly, their objective is not specifically to re-direct investment from the brown to the inclusive green economy but, more generally, to facilitate investment for ‘development’. Thus, there is some ambiguity as what the processes aim to achieve.

In the context of this note, the investment facilitation discussion is mentioned because it is important to ensure that these processes also consider the need to redirect investment to environmentally and socially desirable activities rather than merely encourage more investment into the brown economy. Significantly, the E15 initiative focuses on how to mainstream ‘sustainable’ investment into the everyday work of national Investment Promotion Agencies (IPAs), which aim to attract investment at the national level. Unless environmental and social considerations are appropriately taken into account in such discussions, investment facilitation could become a step backward rather than forward. However, suitably framed, the investment facilitation processes could serve to bring IPAs, who are key players in investment promotion, into the broader discussion about re-directing investment towards environmentally and socially desirable activities.

THE OECD’S STATEMENT ON HARNESSING FREEDOM OF INVESTMENT FOR GREEN GROWTH

Other initiatives have focused on the international sphere, addressing in particular the role of IIAs in promoting sustainable development. For example, in 2011, the States of the Organisation for Economic Co-operation and Development (OECD) adopted the ‘OECD Statement on Harnessing Freedom of Investment for Green Growth’ (OECD Statement), which emphasized the importance of:

- ‘mutual supportiveness of international environmental law and investment law’;
- ‘monitoring investment treaty practices regarding the environment’;
- ‘encouraging business contribution to greening the economy’; and
- ‘spurring green growth through FDI [foreign direct investment]’.¹⁶

However, the OECD Statement places a stronger emphasis on investment protection, which may be due to the fact that it was adopted well before the 2030 Agenda. This perception is supported by the fact that the OECD Statement also emphasizes the importance of ‘strengthening compliance with international investment law through prior review of proposed environmental measures and through effective environmental law and regulatory practices [and] vigilance against green protectionism’.¹⁷

IISD AND UN ENVIRONMENT’S WORK ON IIAS AND SUSTAINABLE DEVELOPMENT

Some other international initiatives have more clearly expressed the idea that sustainable development is the end goal and investment promotion and protection is a means to achieve that goal. For example, the International Institute for Sustainable Development (IISD), a non-governmental organization, already developed the Model International Agreement on Investment for Sustainable Development (IISD Model) back in April 2005.¹⁸ The IISD Model emphasizes the right of States to regulate for social and environmental matters and even includes a chapter setting obligations for investors.

In a subsequent effort, UN Environment and the IISD jointly developed a ‘Sustainability Toolkit for Trade Negotiators,’ which contains a number of sustainable development clauses included in investment chapters of FTAs.¹⁹

In both efforts, the focus is clearly on the international level, i.e. on the reform of IIAs. Significantly, the reforms recommended, and the tools offered, predominantly relate to the post-entry stage of the investment process. The discretionary power of States as to whether to admit investment or not (market access) is fully preserved. The IISD Model and the tools offered in the toolkit focus instead on how to ‘treat’ investment once it has already gained access to the host country. This is another important difference between these initiatives and the OECD Statement, which also focused on market access (i.e. freedom of investment).

SCC – STOCKHOLM TREATY LAB

Some other initiatives focusing on the international level have been launched by the investment arbitration community. For example, the Stockholm Chamber of Commerce (SCC), which handles many arbitrations brought by foreign investors against host States, launched the ‘Stockholm Treaty Lab’ in 2017, an innovation contest that challenged different teams to draft a model investment treaty capable of encouraging investment in climate change mitigation and adaptation.²⁰

What is noteworthy about this ongoing initiative is that it reflects the extent to which the legal services sector is aware of the need to reform IIAs to make them more suitable for the environmental challenges that the world faces today.

UNCTAD'S POLICY TOOLS FOR SUSTAINABLE DEVELOPMENT-ORIENTED IIA REFORM

Perhaps the most comprehensive work undertaken in this area, which covers both domestic and international policies, was launched in 2012 by UNCTAD. In its 2012 World Investment Report, UNCTAD launched the 'Investment Policy Framework for Sustainable Development' (IPFSD) with the aim of bringing together investment policies and the economic, social and environmental aspects of development.²¹ The IPFSD comprised of three components:

1. 'Core principles for investment policymaking';
2. 'National investment policy guidelines'; and
3. Several 'policy options' to design IIAs.

The core principles clarified that foreign investment must lead to inclusive growth and sustainable development and therefore that investment may not be regarded as an end in itself. The national policy guidelines and policy options proposed by the IPFSD specifically called for governments to negotiate 'sustainable development-friendly IIAs' and provided a detailed analysis of how certain standards and terms commonly employed in IIAs can operate so as to make room for sustainable development considerations.

The IPFSD was revised in 2015²² and complemented by another policy tool, the "Road Map for IIA Reform", which focused mainly on the substance of IIA reform ("**Phase 1 of IIA Reform**").²³ The Road Map set out five priority areas for reform, notably: i) safeguarding the right to regulate in the public interest while providing protection; ii) reforming investment dispute settlements to address the legitimacy crisis of the current system; iii) promoting and facilitating investment; iv) ensuring responsible investment to maximize the positive impact of foreign investment and minimize its potential negative effects; and v) enhancing the systemic consistency of the IIA regime so as to overcome the gaps, overlaps and inconsistencies of the current system and establish coherence in investment relationships.

UNCTAD's subsequent stocktaking of reform efforts showed that while key reform options were increasingly incorporated in new IIAs, policy attention needed to focus also on how to modernize the stock of over 2,500 existing old-generation treaties. UNCTAD responded to this policy need by analysing and discussing 10 reform mechanisms as part of "Phase 2 of IIA Reform" in its 2017 World Investment Report.²⁴ Finally, UNCTAD's World Investment Report 2018 presented policy options to enhance the coherence of IIAs with national investment policies and other bodies of international law affecting investment ("**Phase 3 of IIA Reform**").²⁵

More recently, UNCTAD's Reform Package for the International Investment Regime (updated 2018 version)²⁶ brought together UNCTAD's recommendations for these three phases of reform, covering the full range of policy options, and the pros and cons in the design of new, as well as the reform of existing older IIAs. Although the Reform Package goes beyond the more specific topic addressed in this document and not all of its options and recommendations are specifically intended to protect the environment or to promote the transition to inclusive green economies, they are nevertheless relevant and, significantly, they are part of a broader plan with a road map for the steps to be taken.

CONCLUSION

These various initiatives reflect that investment, including FDI, and sustainable development, are increasingly recognized as closely interrelated issues. In particular, more recent initiatives have clarified the relationship between investment-related policies (or 'means') to the ends pursued (i.e. the promotion of sustainable development and the transition to inclusive green economy pathways). We thus see a recognition at the international level that domestic and international investment law should not limit the space within which sustainability policies can be developed and adopted.²⁷ Rather, whenever investment agreements hinder sustainable development or the transition to inclusive green economy pathways, they should be reformed. Indeed, when there is inconsistency between the overall goal pursued and the means to achieve it, it is the means and not the goal that require adjustment. Therefore, in order for investment policies and, in particular, for IIAs to realize their potential as an instrument to promote sustainable development and encourage the transition to inclusive green economy pathways, they must be suitably reformed to allow for sufficient policy space.

III. OPPORTUNITIES AND CHALLENGES

Investment policies, and, in particular IIAs, present opportunities but also challenges for a country's ability to pursue an inclusive green economy pathway. In this section, opportunities arising from IIAs for countries transitioning to inclusive green economies are outlined. Subsequently, it discusses the risks and challenges that countries need to address in order to realize the potential of IIAs to act as vehicles for sustainable development.

OPPORTUNITIES

In the 2014 World Investment Report, UNCTAD estimated the annual amounts needed to realize the SDGs would be US\$ 5-7 trillion.²⁸ This estimation includes the costs of more resilient and adequate infrastructure, the transition from fossil fuel-based to clean sources of energy, the development of adequate water and sanitation systems, and the move towards forms of agriculture that are less reliant on chemicals and fossil fuel-based energy. The massive scale of the financial resources required reflects the equally enormous scale of the transformation needed. All major sectors (including energy, food, water, transportation, construction, chemicals, waste treatment) and all related services (financial as well as many others) are concerned. Moreover, for this transformation to be inclusive, those sections of the population that are currently engaged in sectors that will undergo fundamental change must be given the chance to participate in the transformation and not be left behind.

From the perspective of investment policy, the sheer scale of the transformation required has two main implications. Firstly, public funds, whether public budgets, official development assistance (ODA) or financial support from multilateral agencies (e.g. the World Bank, the regional development banks, the GEF, the GCF) will not be sufficient to meet the financial needs of the transition. Secondly,

to be realistically achieved, the scale of finance to be mobilized cannot rely on considerations of equity only but will also need to appeal to considerations of profitability.

Both implications point to the key role of the private sector, including private sector investment, in promoting sustainable development. In this context, the main opportunities presented by investment policies and, particularly, by IIAs lie in their ability to shift investment²⁹ towards more sustainable alternatives. The ability of IIAs to promote investment remains debated because foreign investment decisions are based on many considerations, and the existence of an IIA is not necessarily sufficient to drive the decision.³⁰ Nevertheless, it may be a useful instrument, particularly to influence the quality, not just the quantity, of investments that are encouraged.³¹

Investment policies, including IIAs, provide a reliable legal framework for long-term investment decisions. This stability can facilitate decision-making by companies and improve their ability to secure the necessary funding from financial intermediaries to enable their investment.

Moreover, from the perspective of host countries, foreign investment in

sustainable alternatives is closely related to additional potential for trade for two main reasons: Firstly, production processes have become globalised with different entities based in different countries focusing on specific components of an overall production process. This phenomenon is summarised in the concept of global value chains (GVCs).³² Foreign direct investment can help a country's industrial sector participate in GVCs.

In this context, investment and trade agreements (global, regional or bilateral) are closely interconnected. Investments may be incentivized not only by the existence of a suitable IIA but also by the import/export possibilities unlocked by trade agreements, which are key to keep the GVC in operation. Trade agreements can

More sustainable investment alternatives may include, among many others:

- Energy: electricity produced from renewable sources, renewable energy equipment, related services, more efficient and flexible – so-called ‘smart’ – electrical grids, related appliances such as ‘smart’ meters, better performance batteries.
- Food: sustainable and organic agriculture, sustainable aquaculture and marine-capture fisheries, sustainable land-use and forestry practices.
- Water: efficiency appliances, water treatment and depollution technologies, investment in water distribution.
- Transportation: hybrid and electric vehicles, public transportation.
- Construction: energy-efficient buildings, resilient infrastructure.
- Chemicals and waste sectors: reduction of waste generation, waste treatment, waste reuse as input for energy production, etc.

facilitate access to the inputs necessary for production processes or the ability to export the component produced in one country to another, where the next stage of production is based. The existence of an IIA can reduce the risk of the investment scheme to produce a certain component in a given country.

Secondly, foreign investment can help a country to diversify its economy, to realize untapped potential and to potentially 'leapfrog' and become a leader in new green industries, with the ensuing potential for poverty reduction, more and better jobs, technology transfer and green exports. However, not all types of foreign investment will make a positive contribution to the host country. In this regard, investment policy, whether at the domestic level or in IIAs, can serve as a means to attract and protect the right type of foreign investment. One major challenge is identifying what type of foreign investment can promote sustainable development and support a country's transition to inclusive green economy pathways. Another major challenge is introducing sustainability requirements without discouraging foreign investment or redirecting it towards less demanding countries. Yet another challenge is designing and using IIAs to encourage foreign investment that is conducive to sustainable development rather than socially and environmentally damaging. These three issues will be addressed in turn later. Before addressing these questions however, it is necessary to first identify the main challenges arising from the use of investment policies, particularly IIAs, as an instrument.

CHALLENGES AND RISKS

Promoting foreign investment through techniques, such as investment contracts, domestic investment laws and, above all, IIAs, has come under much criticism in recent years as a result of the surge in disputes brought by foreign investors against host countries.³³ One of the main concerns underlying this criticism is that the system has been used by foreign investors to seek excessive protection against normal and legitimate regulatory change. Legitimate environmental measures, such as the creation of a natural preserve, the non-renewal of environmental permits, the phasing out or the prohibition of harmful chemical substances, requirements of land decontamination, liability actions for environmental pollution, and many other similar measures have been challenged by foreign investors as a violation of investment protection standards. Each dispute must, of course, be assessed on the basis of its own circumstances but by and large, many countries – both developing and developed – have found themselves facing claims brought by foreign investors for millions, and sometimes billions, of US dollars.³⁴

Looking only at the publicly known investment disputes with 'environmental components' (e.g. relating to green sectors such as waste treatment or renewable energy, or concerning environmental pollution, or calling for the application of environmental law), their number has increased steeply in recent years.

Figure 1 shows the number of such investment claims filed between 1970 and 2015. Out of the 117 claims in the dataset, more than half of the disputes were raised in 2011 or after, which is consistent with the fact that governments have increasingly adopted measures to protect the environment and transition to an inclusive green economy. Regarding the sectors involved in the litigation, most disputes concern the energy sector (renewable energy generation and the phase-out of nuclear energy), a variety of sectors subject to environmental impact assessments and permits (including extractive industries), the water sector (particularly water distribution), and the waste sector (particularly landfills and waste treatment). Figure 2 provides the sectorial distribution of the entire 117 dataset.

Box 1 provides more specific illustrations of disputes in the water and waste sectors. As a general matter, the water and waste sectors are particularly important from an environmental perspective because, with a growing, urbanizing population, water and waste management infrastructure must be expanded and improved. In some cases, countries lack the knowledge and resources to carry out these improvements domestically and have called upon foreign investors to provide such services. As a business venture, investment in these services requires a long-term horizon to be profitable. In the course of the investment, circumstances may change significantly, including both the political (e.g. the population's perception of the investment and the government's position) and the economic conditions (e.g. macroeconomic stability, exchange rates, economic

BOX 1: REGULATORY ACTION AND INVESTMENT DISPUTES

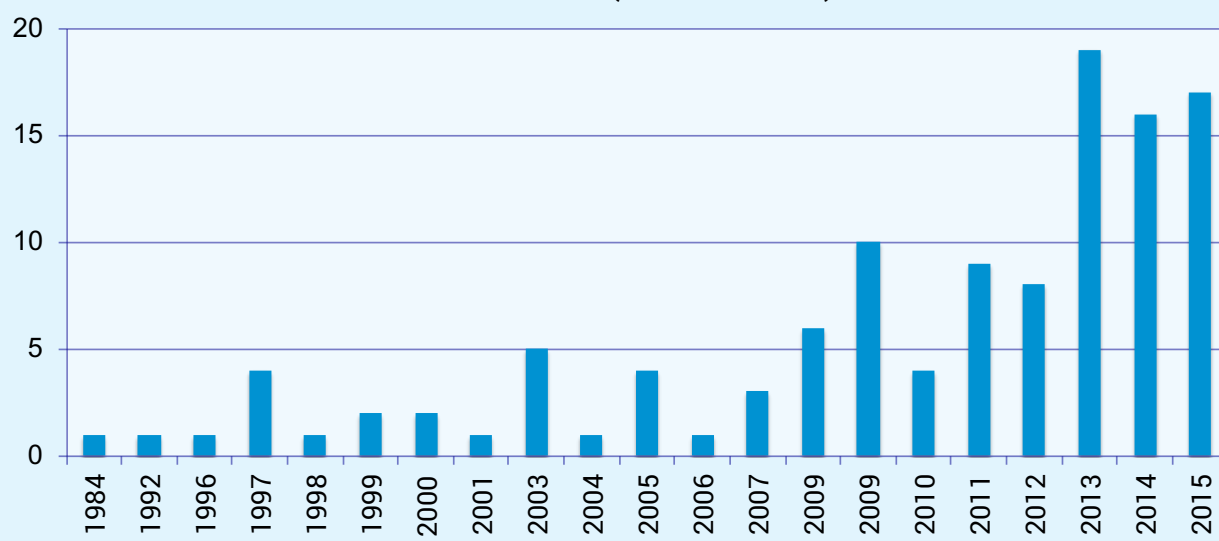
WATER DISTRIBUTION SECTOR

The initial perception of water and sewerage concessions granted to foreign investors is often positive, as they bring a solution to a pressing problem that the local government could not handle effectively and/or efficiently. Investors contribute to the modernization and extension of the infrastructure necessary to provide the service. But a rise in the fees for the services provided or insufficient reinvestment in infrastructure (e.g. to cover the costs for the services provided, or maintain or increase the profitability of the investment despite volatile political or economic circumstances), or, still, changes in the political configuration of the host country, may radically change the perception that the local population or the authorities have of the foreign investor and lead to State actions that in turn trigger a dispute. Such changes have led to investment claims against countries such as Argentina, Bolivia or Tanzania. In virtually all cases, for case-specific reasons, the host State was considered to be in violation of the applicable IIA, even when the measures had been adopted in the context of an economic and social crisis.

WASTE SECTOR

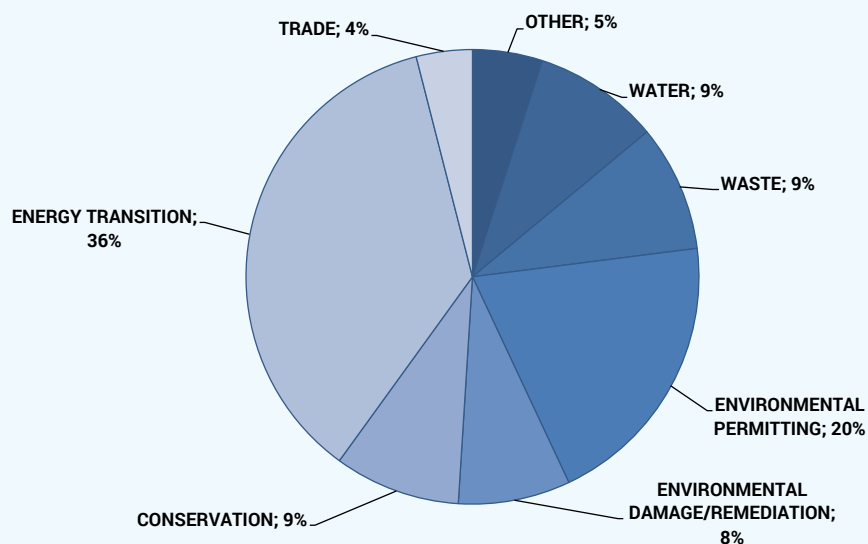
Several developing countries have granted concessions to foreign investors active in the waste treatment and/or management sectors who can bring the necessary technology, know how, experience and financial strength to take over these important environmental services. In some other cases, waste is sent to countries to be treated at a lower cost. Yet, over time, the perception of the investor's activities may change as a result of lack of reinvestment or diligence from the investor's side, or because of public pressure from populations particularly affected by the side-effects of the waste treatment operations. Several investment disputes have been brought in such contexts against countries such as Bulgaria, Canada, the Czech Republic, Mexico or Poland. The outcomes of such disputes have varied. In most of the early disputes, the measures adopted by the host State were considered to be in violation of the applicable IIA.

FIGURE 1: NUMBER OF INVESTMENT CLAIMS WITH ENVIRONMENTAL COMPONENTS (FILED PER YEAR)



Source: Viñuales (2018)

FIGURE 2: SECTORAL DISTRIBUTION OF 117 CLAIMS



Source: Viñuales (2018)

unrest). In several disputes arising from these changing conditions, investors have claimed that measures adopted by States (e.g. the non-renewal of a permit or the freezing of tariffs) amounted to expropriation or were, at least, unfair and inequitable.

Together with non-discrimination standards, such as the so-called most-favoured-nation treatment clause (requiring non-discrimination of foreign investors from different countries) and the national treatment clause (requiring non-discrimination between foreign investors and investors from the host country), the protection against expropriation and the 'fair and equitable treatment' standard are the most frequent bases of claims.

The difficulty with the investment protection provisions in IIAs is that they have to strike a balance between two different types of risk. On the one hand, foreign investors face risks relating to the change of laws, regulations or administrative acts that may have a detrimental effect on their activities (regulatory risk). This risk is however to some extent part of the normal regulatory activity of the State to protect the environment, health and the public good. For this reason, investors, particularly those in regulated industries, should be aware of this, and integrate it into their commercial calculations, as part of their 'business risk'. However, there may be cases in which the State regulatory activity is arbitrary, disproportional or otherwise unfair and would thus be more appropriately characterized as 'political risk'. Importantly, IIAs provide protection against political risk, not business risk. Investment protection standards seek to ensure, for example, that an investment of a foreign investor is not expropriated without appropriate compensation, or that certain foreign investors are not treated less favourably than national economic operators or than other groups of foreign investors or, still, that changes in regulation occur within certain broad fairness parameters.

The line between political risk (against which IIAs provide protection) and business risk (against which no protection is or should be provided by IIAs) is not always clear. Furthermore, the way in which some investment disputes have been decided has tended to blur this line, by considering negative impacts that result from poor or negligent business decisions (e.g. poor understanding of the regulatory environment or continuing the production of a substance despite growing evidence of its potentially harmful effects) as a violation of IIAs. In this way, the normal regulatory activity of the State (e.g. banning a harmful substance, denying or withdrawing an environmental permit, etc.) has been challenged, sometimes successfully, by foreign investors for violation of an applicable IIA. In turn, States have faced ever more legal actions based on IIAs, against the very measures that they are required and encouraged to adopt to protect the environment under MEAs or to transition to inclusive green economy pathways. For this reason, it is important to ensure that IIAs can only be used to challenge unfair action from the host country rather than legitimate regulation. To do so, the scope and operation of IIAs must be made sufficiently clear to ensure that the means (IIAs) are suitable to achieve the ends (sustainable development). The following section discusses how to do so.

IV. MAKING INVESTMENT POLICY WORK FOR SUSTAINABLE DEVELOPMENT

In order for investment policy to contribute to sustainable development and to the transition to inclusive green economy pathways, it must promote a shift of investment from the brown economy to the green sectors discussed earlier, and to do so in an inclusive manner. This, in turn, supposes that the right type of investments, which some refer to as (environmentally and/or socially) 'sustainable' investments, can be identified and that they can be effectively promoted by investment policies. Although this document focuses on IIAs as one investment policy instrument to encourage the right type of investments, a preliminary and very challenging question is how to recognize what these 'sustainable' types of investment are. This question received increasing attention during 2017 in the context of discussions relating to investment facilitation. This discussion, mentioned earlier, will be briefly revisited in the next section before moving into a discussion of the particular role of IIAs in attracting the right type of investment.

Harnessing investment facilitation to redirect investment from the brown economy to an inclusive green economy.

The debate over investment ‘facilitation’ for development has been deliberately framed in such a way as to enable progress without encountering highly controversial issues, such as market access for foreign investment, (post-entry) investment protection by international agreements, or investment arbitration (the so-called ISDS mentioned earlier). The underlying idea, inspired by the trade facilitation context, is that by focusing on efficiency measures and the reduction of transaction costs (i.e. making it less complicated for foreign investors to invest in a country), investment can be effectively promoted. However, beyond this, in order to make a meaningful contribution to countries’ transition to the inclusive green economy pathways, this discussion needs to incorporate considerations on what type of investment should be facilitated.

The basic idea of the investment facilitation discussion is that facilitative measures, which include a variety of regulatory coordination measures, such as ‘one-stop shops’ (where investors can receive all the necessary information and complete most of the paperwork), could be adopted at the domestic level. Investment Promotion Agencies (IPAs) would play a major role in this scenario. But this is not enough because not all forms of investment should be facilitated. Some investments, notwithstanding possible short-term economic benefits, may actually result in an overall negative impact on a country’s prosperity due to negative environmental and social impacts of those investments. For investment to contribute to countries’ transition to inclusive green economy pathways, it is necessary to distinguish between investment in the brown economy and socially and environmentally desirable investment. Only socially and environmentally desirable investments should be facilitated.

Currently, as far as IPAs are concerned, the focus lies on attracting ‘any’ type of investment and the more the better. The calculation of potential benefits (or adverse impacts) only comes later, often at a stage that is no longer linked to the work of IPAs. Underlying this state of affairs is the way in which the performance of IPAs are evaluated, which relies essentially on the amount of capital attracted,³⁵ rather than on the nature and direction of the investment. As a result, IPAs are in competition with one other. In such an environment, IPAs often perceive the application of sustainability criteria to potential investors as a competitive disadvantage, because such criteria may prompt the foreign investor to go elsewhere.

Finding a way to identify and attract the right types of investment is very difficult given that the practices that would have to be changed are deeply rooted in the conduct of both foreign investors and host States (particularly IPAs). The research conducted for this document suggests that eight key inter-related questions need to be addressed, for which further collaborative work is recommended. These sub-questions are identified in Box 2.

SUB-QUESTION	RATIONALE
1. Definition of sustainability criteria for investments ³⁷	The criteria must be able to distinguish investment that contributes to sustainable development from investment that is socially and environmentally harmful. They must be reasonable and strike a balance between the need to attract investment and the need to regulate investment. They could take different forms, including the definition of a core criterion that is extended into more specific criteria by type of sector, product or impact.
2. Standardization of sustainability criteria	The criteria must be standardized to avoid having a different set of criteria for each country or sector, which not only creates major costs and challenges for investors to adapt, but also undermines the effectiveness of the criteria used.
3. How to mainstream these criteria in the investment admission policy	The criteria could be introduced as part of a service provided by IPAs to prospective investors, to the extent that investors should, nowadays, be well aware of the overall trend towards sustainable development and the transition to inclusive green economy pathways.
4. How to ensure that the criteria are meaningfully applied	The meaningful implementation of sustainability criteria should take place not only at the stage of investment admission but also throughout the life of the investment, as sustainability is not a one-off tick in the box.
5. How to ensure that the use of these criteria does not entail a competitive disadvantage	To avoid IPAs playing unfairly and lowering standards to attract investment, these criteria should be standardized in both their content and their level of implementation by IPAs. Thus, the criteria would become part of the level playing field and IPAs would compete on other fronts. For this to be possible, the way in which IPAs are evaluated would have to be changed to take into consideration sustainability criteria in addition to capital attracted, and such a change would have to be adopted and applied in a coordinated manner.
6. What instruments or legal avenues should be employed to state these criteria	Different instruments could be used to set sustainability criteria ranging from soft-instruments, to regulations, to references in domestic law to such instruments, to international trade or investment treaties.
7. Which stakeholders and what process should be considered to develop and mainstream these criteria	In order for the process to be both legitimate and effective, it would have to be developed through a forum that integrates not only government representatives (including IPAs members) and the private sector, but also other stakeholders. The structure of the process would have to ensure that discussions are constructive and reasonable to avoid becoming an arena to vent controversies.
8. Implications of meeting the sustainability criteria	It is critical that meeting or not-meeting (or different degrees in between) the sustainability criteria has practical consequences in terms of both incentives and disincentives (which may range from more favourable access to sustainable public procurement markets, facilitated approval processes, tax advantages/disadvantages, regulatory sanctions, etc.). The possibility to grant such advantages, which amounts to treating certain investments better than others, would have to be clarified in any investment and trade agreement that may potentially apply.

BOX 2:
MAIN AREAS FOR
FURTHER WORK
TO HARNESS
INVESTMENT
FACILITATION
TO REDIRECT
INVESTMENT
FROM THE BROWN
ECONOMY TO AN
INCLUSIVE GREEN
ECONOMY

As suggested by the rationales underlying each question, there are many points of contact between domestic investment policy and international agreements, particularly IIAs. IIAs could play a major role in ensuring that sustainability criteria are meaningfully used by IPAs and, perhaps more importantly, by attaching significant consequences to the conformity with sustainability criteria (by requiring investors' respect as a condition to benefit from the protection of the IIA and making sufficient room in IIA clauses to treat investments with a higher social and environmental contribution more favourably than investments with a lower one). These connections between the domestic and the international levels as well as the further elaboration of the eight questions identified in Box 2 would require further work, as recommended by this document.

IIAs AS INSTRUMENTS TO PROMOTE SUSTAINABLE DEVELOPMENT

In order for IIAs to promote and protect not 'any' type of foreign investment but foreign investment that contributes to sustainable development, IIAs must be designed and applied so as to reserve sufficient policy space for governments to regulate as well as to incentivize investment in sectors that are conducive to sustainable development and inclusive green economy pathways. Carving out space for States to adopt legitimate regulatory action for environmental, human and social wellbeing can be seen as a pre-condition for countries to adopt the necessary domestic policies (such as green industrial policies), to shift investment from the brown to inclusive and green sectors without violating investment protection standards in IIAs. IIAs however can do more than just make room for domestic action; they can also be used as a policy instrument to incentivize certain types of investments that are desirable from a social and environmental perspective. However, putting this potential of IIAs into practice, will rely on reforming the way that IIAs are currently designed and applied. With this in mind, the next section will provide some further background on the structure and operation of IIAs, before turning to the question of IIA modernization and (re-)design.

As noted briefly in the introduction to this note, IIAs – whether they are BITs or investment chapters in FTAs – broadly consist of three components:

1. The characterization of protected investments;
2. The formulation of standards of investment protection; and
3. A dispute settlement mechanism.

The first component is a definition of the scope of protected investments. As already noted, this requires a definition of what constitutes an 'investment' of a 'foreign' investor. There have been vivid debates over what exactly should be considered an 'investment'. One aspect of that debate has concerned the interpretation of the 1965 Convention establishing the International Centre for Settlement of Investment Disputes (ICSID Convention).³⁷ This Convention has

sometimes been interpreted in a way that requires the investment at stake to contribute to the development of the host State³⁸ to access its arbitration mechanism. The scope of protected investments may also be limited by considerations of legality (whether the investment has been made 'in accordance with domestic law'), among many other considerations.

The second component is a list of investment protection standards, which are often formulated in very similar terms across IIAs. The most common standards have already been mentioned; they include:

- The protection against unlawful expropriation (i.e. an expropriation which does not pursue a public purpose, is discriminatory, or is not followed by prompt, adequate and effective compensation);
- The obligation to provide fair and equitable treatment to the investments of foreign investors (a very broad standard of regulatory fairness, protecting investors against arbitrary and unreasonable changes that may frustrate legitimate expectations tacitly or explicitly set by the host State prior to the investment); and
- The obligation to not discriminate between the investments made by investors from different countries (the most-favoured-nation or **MFN clause**) or between domestic and foreign investors (the national treatment clause), among other standards.

The third component frequently consists of an arbitration clause by which the host country consents to submit any dispute arising under the IIA to an international arbitration tribunal involving three (but sometimes also one or five) private individuals acting as arbitrators.

This simple characterization of IIAs provides the necessary basis to understand how IIAs could be (re)designed to provide sufficient regulatory space for States and to incentivize socially and environmentally sustainable investment. As a general matter, it must be noted that, starting in the mid-1990s, the inclusion of a variety of environmental clauses in IIAs became increasingly frequent. Although only a minority of the entire body of more than 2500 IIAs contain such clauses,

1. General language in preambles that mentions environmental concerns and establishes protection of the environment as a concern of the parties to the treaty.
2. Reserving policy space for environmental regulation.
3. Reserving policy space for environmental regulation for more specific, limited subject matters (performance requirements and national treatment).
4. Provisions that clarify the understanding of the parties that non-discriminatory environmental regulation does not constitute 'indirect expropriation'.
5. Provisions that discourage the loosening of environmental regulation for the purpose of attracting investment.
6. Provisions related to the recourse to environmental experts by arbitration tribunals.
7. Provisions that encourage strengthening environmental regulation and cooperation.

**BOX 3:
TYPES OF
ENVIRONMENTAL
CLAUSES IN IIAs**

Source: OECD
(2011)

most recent IIAs contain environmental clauses or even entire sustainable development chapters. A study published by the OECD in 2011³⁹ and covering 1623 IIAs involving OECD Member States (i.e. over half of all IIAs globally) concluded that only eight per cent of all the IIAs surveyed contained an explicit reference to environmental protection, but since the middle of the 1990s 'the proportion of newly concluded IIAs that contain environmental language began to increase moderately, and, from about 2002 onwards,' rose steeply, and has continued to increase since.⁴⁰ Box 3 summarizes the main types of environmental clauses found in IIAs.

Two more recent studies published in 2014,⁴¹ prepared by UNCTAD and the OECD respectively, confirm the trend suggested by the 2011 OECD Report. Interestingly, the 2014 OECD Study also sheds light on the reasons why such environmental provisions are included in IIAs. As a general matter, the report finds that such clauses are included as a result of commitments made by governments in domestic legislation and/or policy instruments. This is the case, according to the findings, in Australia, Canada, Chile, Japan, New Zealand, the United States, and the Member States of both the European Free Trade Association and the European Union.⁴² In turn, these domestic or regional commitments pursue a variety of policy objectives, which are discussed in more detail in Box 4.

As suggested by the previous discussion, treaty practice is rapidly evolving to reflect the increasingly well-recognized SDGs and the clear mandate issued by the 2030 Agenda. An example that showcases some innovative features towards integrating sustainable development considerations into IIAs is the 2016 Morocco-Nigeria BIT,⁴³ summarized in Box 5.

However, the operation of IIAs is not only driven by their drafting or design. Equally important is the way in which they are interpreted and applied. This opens a very controversial debate relating to investment disputes decided by investment arbitration tribunals. The debate has led several countries and groups of countries, including the EU and Canada, to support a far-reaching reform of the investor-State dispute settlement system (ISDS), including the creation of permanent investment courts. This is largely due to:

1. Inconsistent decisions in very similar factual and legal situations,
2. The perception of a bias in favour of investors and, more generally,
3. The legitimacy deficit of tribunals formed by one or more private persons for a specific dispute and making decisions on matters that have a significant, sometimes major, public dimensions.

For the purpose of this document, it is important to highlight the following points. Some of the environmental clauses discussed in the previous paragraphs are already being applied to grant host States more space to manoeuvre for environmental regulation. Examining such clauses in investment arbitration tribunals is still relatively rare when compared to the growing number, as well as

A study published by the OECD in 2014 suggested that the main reason why countries and regional economic integration groups use environmental and sustainable development clauses in FTAs is to respond to commitments in domestic legislation and/or policy instruments. In turn, these commitments may pursue a variety of objectives. The study surveyed the answers provided by ten delegations (representing a total of 31 countries) of the OECD Joint Working Programme on Trade and Environment. The four policy objectives identified were the following: (1) to contribute to the overarching goal of sustainable development; (2) to ensure a level playing field among Parties to the agreement; (3) to enhance co-operation in environmental matters of shared interest; and (4) pursuing an international environmental agenda.⁴³ Significantly, the survey showed that the objective most frequently pursued by the use of environmental and sustainable development clauses is to ensure a level playing field among trading partners. The objective of promoting sustainable development came second, by a slight margin. The methodology used in the study is not conclusive and leaves room for several interpretations. However, it can be broadly concluded that there is evidence that environmental protection and sustainable development are most often sought to ensure better trade liberalization rather than the other way around. This finding highlights the need for a more balanced approach that reflects the current views of the international community as reflected in Agenda 2030. With this new mindset, trade and investment are not goals to be pursued as ends in and of themselves, irrespective of their social and environmental effects. They are means for pursuing sustainable development and the transition to inclusive green economy pathways, and trade and investment agreements should be designed to reflect this order of priorities.

BOX 4: POLICY OBJECTIVES DRIVING THE USE OF THE ENVIRONMENTAL CLAUSES IN FTAs

Source: OECD (2014)

the increasingly ambitious scope, of such clauses. Nevertheless, it is starting, and in a context where changing the mindset of negotiators and arbitration practitioners is as important as changing the law, this is an encouraging sign. Box 6 discusses a case where the arbitration tribunal relied extensively on environmental clauses to reject the claim of the investor.

However, environmental clauses are not, for now, the main instrument used to shield environmental and sustainable development policies from challenges by investors for violation of an IIA. Instead, general concepts of investment law have played a much greater role in previous cases, as interpretations of general provisions or concepts of investment law have made it possible to carve out significant space for sustainable development regulations. Concepts such as the following can all be – and have all been – used to shield State action from investment claims:⁴⁴

- The police powers doctrine (which recognizes the right and duty of countries to regulate for the common good);
- The definition of ‘like circumstances’ in the context of non-discrimination standards (that is, an investor whose investment is more harmful to the environment is not in ‘like circumstances’ with an investor that has a lower environmental footprint, and can be treated differently);
- The diligence of investors in forming their expectations and assessing the applicable regulatory framework (which requires investors to assume the risk of regulatory change if it is foreseeable or if it is a normal occurrence in a

**BOX 5: INNOVATIVE
FEATRES OF THE
2016 MOROCCO-
NIGERIA BIT**

The Morocco-Nigeria BIT was signed in December 2016 and, although it is not yet in force, it contains some innovative features that are worth mentioning. As a general matter, the treaty makes clear that its goal is the pursuit of sustainable development and it contains several references to sustainable development in the preamble. Some other features worthy of noting are the following:

[1] Definition of investment: the term investment requires a contribution to sustainable development (Article 1(3)).

[2] Regulatory powers: the treaty contains express reservations of the regulatory powers of the States, including the right to exercise discretion 'with respect to regulatory, compliance, investigatory, and prosecutorial matters and to make decisions regarding the allocation of resources to enforcement with respect to other environmental matters determined to have higher priorities' (Article 13(2)). Moreover, it provides that nothing in the treaty prevents a State party from adopting, maintaining, or enforcing, in a non-discriminatory manner, any measure otherwise consistent with the treaty that they consider appropriate to ensure that investment activity in their territory is undertaken in a manner sensitive to environmental and social concerns (Article 13(4)).

[3] Obligations for investors: the treaty includes a range of obligations relating not only to environmental protection but also to social, labour and human rights, among other considerations. Investors are required to comply with environmental assessment screening and assessment processes in accordance with the most rigorous of the laws of either the home or the host State (Article 14(1)), as well as to comply with social impact assessments based on standards agreed within a Joint Committee consisting of government representatives (Article 14(2)). Like the host countries, investors must apply the precautionary principle (Article 14(3)). They must maintain an environmental management system and uphold human rights in accordance with core labour and environmental standards as well as labour and human rights obligations of the host country or the home country (Article 18). They must not engage or be complicit in corruption practices, and they must meet or exceed national and internationally accepted standards of corporate governance (Article 19). They are also expected to operate through high levels of socially responsible practices and to apply the ILO Tripartite Declaration on Multinational Investments and Social Policy (Article 24), and they 'should strive to make the maximum feasible contributions to the sustainable development of the host State and local community' (Article 24(1)). Finally, the treaty provides for the liability of investors before the courts of their home country for decisions made in relation to the investment that lead to significant damage in the host country (Article 20).

Source: Gazzini
(2017)

**BOX 6: AL TAMIMI
V. OMAN (2015)**

The interpretation and application of environmental clauses contained in an IIA arose in a case brought by a US investor against Oman, under the US-Oman FTA. The case concerned the enforcement of domestic environmental laws in relation to extractive industries, specifically a limestone quarry investment. The dispute was brought before an investment arbitration tribunal for violation of the investment protection standards of the applicable IIA. In assessing the merits of the claim, the tribunal relied both on Article 10.10 (an environmental policy reservation provision in the investment chapter of the treaty) and Chapter 17 (the environmental chapter of the treaty) to interpret the international minimum standard of treatment in Article 10.5 of the treaty (the applicable investment protection standard), which, according to the investor, the host State had violated. Significantly, the tribunal noted that:

‘[When] it comes to determining any breach of the minimum standard of treatment under Article 10.5, the Tribunal must be guided by the forceful defence of environmental regulation and protection provided in the express language of the Treaty’ (para. 389)

This consideration was key in leading the tribunal to reject the investor’s claim for violation of Article 10.5 of the treaty.

- regulated sector);
- The legality of the investment in accordance with the domestic laws of the host country at the time it is made (including the need to secure the relevant environmental permits);
 - The use of State counter-claims for the environmental harm caused by the investor; and
 - The operation of some specific clauses which exempt State action for national security or at least excuse such action (clauses that have been interpreted to apply to environmental and social concerns).

In order to illustrate this point, [Box 7](#) discusses two concepts, namely the police powers doctrine and legality clauses. The foregoing discussion suggests a number of ways in which IIA design and operation could promote sustainable development.

From a design perspective, introducing explicit environmental and sustainable development language in the text of the treaty is a useful step. There are a range of techniques to do this, from including language in the preamble or

THE POLICE POWERS DOCTRINE

The police powers doctrine is a well-known concept of international law that recognises that sovereignty States have both the right and the duty to regulate for the common good. The terminology 'police powers' is taken from the United States practice, which is itself derived from 18th and 19th European practice. Police in this context comes from 'police' in French, which in this meaning is conveyed by the word 'policy' in English. Its main application in the context of investment disputes – much as in a domestic context – is to emphasise that no compensation can be claimed for the negative impact on property of measures adopted as part of the normal regulatory rights and duties of States. In basic terms, it means that State action for the common good is part of normal life and, as far as investors are concerned, it is part of their business risk, for which they are solely responsible. This doctrine has been used in a number of disputes with environmental components. Two of them, *Methanex v. United States* and *Chemtura v. Canada*, both relating to environmentally harmful chemical substances, have clarified its application in an environmental context.

LEGALITY CLAUSES

Many IIAs condition the protection of an 'investment' from a foreign investment to the requirement that the investment is made 'in accordance with the laws of the host State'. Such legality clauses, which in some cases have been considered to be implicit in every investment treaty, may have a significant impact on the protection of investments that are socially or environmentally unsustainable. The operation of such clauses, as interpreted by investment tribunals, relies on two distinctions. The first concerns the moment when the investment is made. If the investment is illegal at the time it is made, the investment is not protected by the treaty and the tribunal cannot or should not hear the claim. If it only becomes illegal later, the tribunal should hear the claim but it will take into account the illegality in deciding the merits. The second distinction concerns the laws to be considered when assessing the illegality. Initially, tribunals only excluded extreme cases of illegality, such as corruption or violation of the so-called international public policy. Over time, they have tended to expand the relevant set of laws, first to the investment laws of the host State and, more recently (e.g. in *Mamidoil v. Albania*) to a range of laws, including environmental permitting laws.

BOX 7: THE USE OF GENERAL CONCEPTS OF INVESTMENT LAW TO SHIELD ENVIRONMENTAL REGULATION

broad policy reservation clauses, to more specific ‘carve-outs’ in investment protection standards (e.g. stating that, as a rule, environmental regulation does not constitute an expropriation), to extensive environmental and sustainable development chapters in the text of the treaty. Some current trends, summarized to some extent by the 2016 Morocco-Nigeria BIT, suggest some other techniques, such as: requiring that investments contribute to the sustainable development of the host country (in order to be covered by the definition of investment of the treaty), requiring that Joint Commissions be established with representatives of State parties, and chapters setting out the obligations of investors with respect to both environmental and social development.⁴⁵ Careful drafting of IIAs can also help countries to make best possible use of instruments that can help bridge the SDG-financing gap such as public-private-partnerships (PPPs), by reducing risk of PPP-related ISDS cases.⁴⁶

In terms of interpreting and applying IIAs, the new design features are already exercising some influence in practice, as suggested by cases such as *Al-Tamimi v Oman* (see Box 6). But it is also very important to keep in mind the potential of general concepts of investment law (police powers doctrine, like circumstances, investor diligence, legality clauses, counter-claims or emergency and necessity clauses), which, if appropriately interpreted can make a very useful contribution to a more balanced operation of IIAs. Supporting this dimension is possible through a combination of institutional reform and appropriate training. On institutional reform, the efforts of several arbitration institutions, including ICSID, to make the decisions of investment tribunals less erratic and to contribute to their increased legitimacy (e.g. by creating an ‘appellate body’ capable of harmonising investment jurisprudence or by replacing investment arbitration by more legitimate and more consistent investment courts), may also be relevant for making IIAs work for sustainable development, but they belong to a wider debate on the reform of the entire investment regime. Regarding training, it is important to equip government officials in charge of international litigation with the necessary tools to select suitable arbitrators, draft memorials and other acts, and conduct litigation proceedings, as well as to ensure that sustainable development arguments are properly used in litigation. This was expressly recognized in the Addis Ababa Agenda, which articulated the need to ‘offer ... advisory support in investment-related dispute resolution.’⁴⁷

Last but not least, reforming IIAs is a very important enabler for countries to implement green industrial policies to transition to inclusive green economies. Green industrial policy has been the object of several significant initiatives from Partnership for Action on Green Economy (PAGE) partners in recent years.⁴⁸ It is important to highlight that in developing green industrial policies, governments – from the national to the local level – must be mindful to take obligations under international law, including those by IIAs, into account in their overall assessment of green industrial policy design. This is not to subordinate environmental policy to IIAs but only to highlight that the pursuit of environmental objectives should be achieved to all the extent possible in a manner consistent with

international obligations. UN Environment has developed a number of tools for integrated policy assessment, particularly *Integrated Policy-Making for Sustainable Development. A Reference Manual (2009)* and *Guidelines for conducting Integrated Environmental Assessments (2017)*.

In order to harness the potential for IIAs to promote inclusive green economy pathways, they can be linked to efforts for facilitating investment in environmentally and socially desirable activities. As such, IIAs may be used as an instrument to channel investments and encourage 'sustainable' investments versus investments that are linked to negative environmental and social impacts, for example by attaching significant consequences to the level of conformity of an investment with sustainability criteria. This could be achieved by linking sustainability criteria to the definition of investment or within the legality clauses in IIAs. Another option can be to enable host countries, through a range of environmental clauses in IIAs, to treat socially and environmentally desirable investments more favourably than investments in brown sectors.

V. LOOKING AHEAD

The purpose of this concluding section is to pull together the threads of the different sections of this document and provide recommendations for further action. The following four recommendations have been derived from the discussion in this document and its underlying research:

1. States – particularly, but not only, through their IPAs – as well as other relevant stakeholders (e.g. the private sector, standard-setting organizations, international organizations and civil society) take steps to facilitate the shifting of investment from the brown economy to socially and environmentally desirable sectors and activities. More specifically, it is recommended that:
 - States seek to identify and implement, through appropriate processes, common sustainability criteria to channel investment into socially and environmentally desirable activities; and
 - In order to effectively implement these criteria, the performance evaluation of IPAs should not be narrowly focused on economic aspects (e.g. amount to capital attracted) but expanded to take into account the overall contribution of the investment to sustainable development.

2.

Governments – particularly treaty negotiators – pursue and expand their reform agenda for IIAs to ensure that sustainable development considerations are sufficiently reflected in the text of IIAs. The goal of reform is to make space for policies necessary to shift investment towards inclusive green economy pathways, as well as to incentivize investment specifically in sustainable alternatives within the energy, food, water, transportation, construction, chemical, and waste sectors. For these purposes, it is recommended that:

- States continue to use references to sustainable development in the preamble of IIAs and include clauses reserving environmental policy space; and
- States aim to:
 - > Clarify that investments are a means towards the goal of sustainable development;
 - > Limit the protection of IIAs to investments that contribute to sustainable development (through investment definition and legality clauses);
 - > Use carve-out clauses excluding, in principle, sustainable development policies from the scope of (certain) investment protection standards;
 - > Clarify and strengthen the requirement of investor diligence, including, among other things, through chapters setting investor obligations (crucially, these obligations should be relevant not only to assess the merits of investment claims but also earlier to potentially deny the protection of the treaty); and
 - > Pursue the reform agenda for the investor-state-dispute settlement (ISDS) system by exploring a variety of options, including an appellate body to unify the jurisprudence of investment tribunals, replacing investment arbitration with investment courts, introducing standing committees that can issue general interpretations binding on arbitration tribunals, and developing better channels for transparency and legitimacy (e.g. the Mauritius Convention concluded in the context of the UN Commission on International Trade Law,⁵¹ deontological rules for arbitration practitioners with suitable incentives/sanctions, etc.).

3.

In parallel with the previous two tracks, States, international organizations and other relevant stakeholders, including non-governmental organizations, pursue their efforts to improve the operation of the investment regime, including IIAs. This includes, among other things:

- Clarifying the operation of traditional investment law concepts in a sustainable development context, through studies, meetings and declarations;
- Providing the necessary training to government officials tasked with handling international litigation in their countries;
- A potential step could be adopting joint declarations by all the Parties to an IIA or the ICSID Convention clarifying the understanding of certain terms (e.g. stating the reference to contribute to the development of the host State in the preamble of the ICSID Convention is to be understood as a requirement of the definition of investment and that the term 'development' is understood as 'sustainable development'). Such declarations would constitute subsequent agreements of the Parties, a form of authentic interpretation, and would have to be taken into account in future investment disputes.

4.

These different tracks, which represent the domestic and international levels, can be designed in such a way as to be mutually reinforcing.

- Suitably reformed, as noted in Recommendation 1, IIAs would leave enough room for countries to adopt a variety of inclusive, green industrial policies (e.g. support schemes for cleaner industries, sustainable public procurement). But it is very important that in developing such policies, governments – from the local to national and regional level – are aware of the potential inconsistencies between their policies and their international commitments and vice-versa. Thus, States must consider, when assessing the implications of adopting a new policy, entering a new treaty or modifying an existing one, potential legal inconsistencies and how to address them. States are recommended to integrate this legal dimension into domestic assessment methodologies as well as in those generated by international organizations.
- Another form of articulation is the potential for investment facilitation measures and IIAs to strengthen each other. Narrowing down the protection of IIAs to investments that meet certain sustainability criteria or, at least, allowing for additional advantages to be granted to such investments would be a way of contributing to the implementation of the sustainability criteria managed by IPAs.

ENDNOTES

- 1 See the database built by the UN Conference for Trade and Development (UNCTAD): <http://investmentpolicyhub.unctad.org/IIA> (last visited on 20 December 2017). [\[back\]](#)
- 2 UNCTAD, World Investment Report 2014. Investing in the SDGs (2014), available at: www.unctad.org (last visited on 20 December 2017). [\[back\]](#)
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International investment agreements have the potential to mobilize and channel investment towards inclusive green economic activities.

However, putting the potential of international investment agreements into practice will rely on reforming the way they are currently designed and applied. The way many international investment agreements are designed currently overlooks the importance of environmental and social considerations. Moreover, in their present form and operation, they may restrict the ability of States to implement policies that protect the environment and support a green economy transition.

In order to realize the potential of international investment agreements, they must be designed and applied in a way that reserves sufficient policy space for governments to regulate as well as to incentivize investment in sectors that are conducive to sustainable development.

This policy note examines these interlinkages and provides practical recommendations for reforming the current investment architecture and the design of international investment agreements, towards safeguarding policy space and mobilizing investment for a green economy.

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