Privatizing Human Rights
The Interface between International Investment Protection and Human Rights

1. Introduction

Professor Neuhold’s 65th birthday is a welcome opportunity to pay overdue tribute to him for the counsel and support he has been giving me so splendidly during all those years since I became his assistant in 1995. Whenever I needed his advice he had a listening ear and useful suggestions. He allowed for a large degree of own responsibility and academic freedom. Thank you so much for giving me an opportunity to work in a very challenging and exciting field and guiding me through it for the past eleven years.

Professor Neuhold devoted a substantial part of his academic career to bridging the gap between international law and international relations and encouraged his students and assistants to address issues with an interdisciplinary approach. He taught us never to overlook the political aspects of legal topics. It is in this spirit, that I chose my topic and wanted to address a highly political topic from the perspectives of human rights law and international investment law and to bridge the gap between these two fields of international law.

During the 1990s a trend emerged to privatize the infrastructure in the developing world. Before that development the State or the local communities were in charge of services such as water and sewage systems, electricity supply, public transportation etc. Access of the population to the necessary

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minimum supply of some of these services is protected by economic, social and cultural rights.\textsuperscript{1}

Governments often turned to foreign investors to achieve the privatization of formerly public services. This led to a situation where foreign investors were operating in fields where human rights obligations are incumbent upon States. Put differently, foreign investment is used as an instrument to further the implementation of human rights. So generally speaking it would not be correct to condemn foreign investment in privatized public infrastructure \textit{ab initio} as being in conflict with human rights norms.

However, privatizing the supply of essential services has often led to the false assumption that the responsibility for the realization of these rights has also been subcontracted to the foreign private provider and that the State would no longer be responsible for the realization of the corresponding human rights. On the basis of the economic and social rights standards accepted by the States they are under an obligation to ensure that everyone in their jurisdiction has access to the necessary minimum supply of these services. This is true e.g. with regard to water supply.

Foreign investment is today regulated by a patchwork of bilateral and regional treaties that have proliferated since the late 1950s at an ever-accelerating speed. Today over 2300 bilateral investment treaties (BITs) and several regional treaties that contain norms to protect foreign investment have been concluded.\textsuperscript{2} Over 1700 are in force.\textsuperscript{3} The efforts to agree on a comprehensive multilateral investment agreement have failed. BITs traditionally cover the following key issues: scope and definition of investment, admission and establishment, non discrimination in the form of most favoured nation treatment and national treatment, fair and equitable treatment, full protection and security, compensation in the event of direct and indirect expropriation of the investment, guarantees of free transfers of funds and dispute settlement mechanisms. Dispute settlement is provided for on a State-to-State and an investor-to-State level.

Investment can be made in a wide range of sectors and can take many different forms. Hence investment dispute cases also cover a wide range of investment activities. They have arisen with regard to activities such as construction, water and sewage services, brewing, telecommunication concessions, banking and financial services, hotel management, television and radio broadcasting, hazardous waste management, textile production, gas and oil production, and various forms of mining.

\textsuperscript{1} For instance, Art. 11 CESCR guarantees the right of everyone to an adequate standard of living. See in more detail \textit{infra} section 3.1. The Unclear Scope of Economic, Social and Cultural Rights.

\textsuperscript{2} UNCTAD, Research Note, Recent developments in international investment agreements, 30 August 2005, UNCTAD/WEB/ITE/IIT/2005/1, at 1.

\textsuperscript{3} \textit{Ibid.}, at 7.
Thus it is difficult to generalize the effects of investment on the enjoyment of human rights. As a UN report indicates, well-managed investment has the potential to promote and protect human rights. Today, most developing countries seek investment as a means of promoting development. Accordingly, there is a potential for a positive correlation between foreign investment and human rights. Particularly in the field of economic, social and cultural rights foreign investment can have a positive impact and both fields could be mutually reinforcing.

However, beside this potential to enhance the respect of human rights, a number of human rights problems related to foreign investment have arisen over time and are likely to arise in the future. Human rights related problems may arise in this context in two regards. First, the privatized service supply may not be in accordance with human rights standards. This is, for instance, the case if persons not able to pay for water supply are denied access to a minimum quantity of water. Second, human rights violations can occur as a side effect of the activity of the privatized service providers, such as pollution of the environment in case of a breakdown of sewage systems or waste management facilities.

Furthermore there are other areas, which are not typically linked to the privatization of formerly public services, where human rights problems can arise with regard to foreign investments: for instance cases of ill-treatment by privately hired security services, cases of child labour, or working conditions which violate human rights. Another area of potential conflicts are concession treaties allowing for resource exploitation on indigenous peoples’ lands without respecting the relevant human rights provisions. These cases, important as they are, are not the focus of this contribution.

Human rights issues can also arise at the other side of the equation, namely with regard to investors’ rights. Investors are not only protected against

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6 Ibid., at 8.


expropriation without compensation by BITs, but also to some extent, by regional human rights conventions. Thus there is also a potential conflict between the consumers’ right of access to water and the investor’s right to property. This conflict, however, can be solved within the system of human rights protection. The manner in which this can be achieved shall be looked at very briefly as it can provide a source of inspiration for a possible conflict resolution of the conflicting interests at stake.

The aim of this contribution is first to outline some of the conflict scenarios linked to infrastructure privatization. Second, deficiencies in the clarity of the substantive norms protecting human rights on the one hand and foreign investments on the other hand will be highlighted. The lack of clarity complicates the predictability of a human rights violation on the one hand and the predictability of violations of investors’ rights on the other. Third, this article will focus on the lack of interfaces between the supervision mechanisms of international investment law and international human rights.

2. Scenarios of Potential Conflict

A fictitious scenario will illustrate the complex interaction between privatization of services and human rights. A public utility has accumulated ever-mounting debts and its services were not available to important parts of the population that were not connected to the water supply system. This was especially true for slums in big cities. In some parts where dwellings are connected to the public water supply system, water would not have been available for much of the day, or the water quality was poor. Those without connections to the supply system would have to resort to buy water from tanker trucks which might have been unhealthy and/or expensive. In this situation privatization was chosen to ensure the accessibility of clean water for all at all times. A tender was organised and an international water management company submitted a bid, was selected and finally a concession contract was signed. Thus a foreign investor was asked to provide risk capital to upgrade the water services.

As a consequence of the privatization of the infrastructure, consumers faced higher bills. This can have a variety of reasons, for instance:

- the private supplier has no interest in making debts but has to operate at a profit.
- the private supplier had to accept to repay the previously accumulated debt of the public supplier and roll that cost into the rate structure.
- changes in consumption patterns as a result of increased availability of water.

These higher bills led to public opposition against the concessionaire. Politicians driven by public unrest attempted to renegotiate the concession contract and to
roll back the rates. After failing to renegotiate they terminated the concession. The investor thereupon filed a request for arbitration. The arbitral tribunal has to decide whether the rights of the investor, pursuant to a particular bilateral or regional investment protection treaty have been violated by the State. This could have occurred through regulations or through a cancellation of the concession. We may then be in a situation of a conflict between human rights interests of the population and investment protection norms. The main players in this conflict are the population concerned sometimes supported by civil and human rights movements, the government and the foreign investor.

After this introductory scenario let us turn to two real cases concerned with the privatization of water supply systems.

The case of *Aguas del Tunari, SA v. Bolivia* was similar to the fictitious scenario described above. The dispute concerned a 40-year water-supply contract between a consortium led by International Water and the Bolivian Water and Electricity Superintendencies. Cochabamba is Bolivia’s third largest city. Its water and sewage service was to be privatized under this contract. After the grant of the concession there was significant opposition in various parts of Bolivia, and particularly in Cochabamba. The operation of the new supplier began in January 2000 and the concession was terminated in early April 2000 after major violent protests. The government and Aguas del Tunari tried to reach an amicable settlement. After these negotiations failed Aguas del Tunari in November 2001 filed a request for arbitration with the International Centre for Settlement of Investment Disputes (ICSID). In January 2006 the Government of Bolivia and Aguas del Tunari settled their dispute. They declared that the concession was terminated only because of the civil unrest and the state of emergency in Cochabamba and not because of any shortcomings on the part of the investor. The claims before ICSID were withdrawn. The parties agreed that no compensation would be paid by the Government of Bolivia or Aguas del Tunari for the termination of the concession and the withdrawal of the claim.

The water supply of another big city, Buenos Aires and 17 districts of the Province of Buenos Aires, is at the origin of yet another dispute before an ICSID tribunal. In that case *Aguas Argentinas S.A.* is demanding compensation for the alleged impact on its business of the general economic emergency

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10 *Ibid.*, para. 73.
13 *Aguas Argentinas, SA, et al. v. Argentina*, ICSID Case no. ARB/03/19, Order in Response
measures adopted by the Argentinian government during the 2002 economic crisis. Civil society organizations requested access to the hearings and to the documents produced in the arbitration. Additionally, they requested that the tribunal take into consideration fundamental international and internal rights and standards relating to public health, access to essential services, adequate standards of living, housing and consumer rights. The Tribunal granted an opportunity to the petitioners to apply for leave to make *amicus curiae* submissions in accordance with certain conditions set out by the Tribunal. The case is currently pending.

In both cases the State relied upon foreign investors to provide services with regard to a right where it is under an obligation to ensure that everyone can enjoy this right namely the human right to water. The State was not in a position to fulfil its obligations and thus opted for bringing in a foreign investor. Later on, either as a reaction to higher bills or because of other policy considerations, it wanted to change or terminate the concession agreements. In both cases, the State was potentially in breach of either human rights obligations or investment protection norms or both.

Another scenario where the privatization of formerly public services may lead to conflicts between investors and the State bound by human rights obligations is the field of waste management. Though typically considered from the environmental law point of view such situations may also have a human rights aspect. It is not so much the performance of the service which leads to human rights concerns but side effects of this performance, namely pollution. Human rights become an issue when the facility pollutes its surroundings so heavily that it affects the rights to a home, to privacy and family life of persons living in the neighbourhood of the facility. These rights are for instance covered by Article 8 of the European Convention on Human Rights (ECHR). They have been successfully invoked with regard to pollution by waste treatment facilities and fertilizer factories. It is important to note in this context that although Article 8 ECHR is a classical civil right it can also be used to protect rights like the right to an adequate living standard, which would typically be considered an economic and social right.


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14 Aguas Argentinas, *supra* note 13, para. 23.

15 This right is for instance protected by Art. 11 CESCR, which recognizes the right of everyone to an adequate standard of living, as well by Art. 12 CESCR, which recognizes the right to health. *See* General Comment No. 15 of the United Nations Committee on Economic, Social and Cultural Rights, 26 November 2002, E/C.12/2002/11, The Right to Water. *See* in more detail *infra* section 3.1. The Unclear Scope of Economic, Social and Cultural Rights.

16 Convention for the Protection of Human Rights and Fundamental Freedoms, 5 ETS.


18 *See e.g.* Art. 11 CESCR:
The European Court of Human Rights in *Lopéz Ostra v. Spain*\(^{19}\) dealt with a case where a private waste treatment plant that was built on public land, had received public subsidies, had an operation permit and polluted the environment to an extent that the health of the persons living in the neighbourhood was at risk. The Court stated that the State had a positive obligation to protect the applicant’s right to respect for her home and her private and family life. Thus the State had to balance these interests with the municipality’s interests to operate the waste management facility. The Court held that the municipality violated this right by not striking a fair balance between these conflicting interests. It said:

> Admittedly, the Spanish authorities, and in particular the Lorca municipality, were theoretically not directly responsible for the emissions in question. However, as the Commission pointed out, the town allowed the plant to be built on its land and the State subsidised the plant’s construction (see paragraph 7 above).\(^{20}\)

Having regard to the foregoing, and despite the margin of appreciation left to the respondent State, the Court considers that the State did not succeed in striking a fair balance between the interest of the town’s economic well-being - that of having a waste-treatment plant - and the applicant’s effective enjoyment of her right to respect for her home and her private and family life. There has accordingly been a violation of Article 8.\(^{21}\)

In the following, the issue shall be approached from an investment law perspective. There are several investment arbitration cases relating to waste treatment facilities.\(^{22}\) The human rights implication of this type of privatizations may be analysed by using the case of *Tecmed*\(^{23}\) as an example. In that case the renewable licence to operate a controlled landfill of hazardous industrial waste was not renewed. The State authority further asked the operator of the facility to submit a program for the closure of the landfill. The claimant argued that these modifications were, to a large extent, due to political circumstances essentially associated with the change of administration in the municipality in

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1. The States Parties to the present Covenant recognize the right of everyone to an adequate standard of living for himself and his family, including adequate food, clothing and housing, and to the continuous improvement of living conditions. The States Parties will take appropriate steps to ensure the realization of this right, recognizing to this effect the essential importance of international cooperation based on free consent.


22 See e.g. Tecnicas Medioambientales Tecmed SA v. The United Mexican States, Award, 29 May 2003, 43 ILM 133 (2004); Metalclad Corp. v. United Mexican States, Award, 30 August 2000, 5 ICSID Reports 226.

which the landfill was physically located, rather than with legal considerations. According to the claimant’s allegations, the new authorities of Hermosillo encouraged a movement of citizens against the landfill, which sought the withdrawal or non-renewal of the landfill’s operating permit and its closedown, and which also led to confrontation with the municipality, even leading to blocking access to the landfill. The claimant also stressed that certain breaches of the conditions of the permit had been the object of an investigation by the Federal Environmental Protection Attorney’s Office (PROFEPA). PROFEPA had not found violations of such severity that these might have endangered the environment or the health of the population. The government alleged that the permit was not renewed for the following reasons:

1. the protection of the environment and public health, and 
2. the need to provide a response to the community pressure resulting from the location of the landfill and Cytrar’s violations during the operation, which some groups interpreted as harmful to the environment or the public health.

The ICSID tribunal in the case of Tecmed found a violation of the expropriation norm contained in the BIT.27

We have seen that an extreme situation of pollution of a waste treatment facility can lead to violations of the right to privacy, a home and family life. So far, none of the cases arbitrated were based on facts showing health damages for the population neighbouring the facility.

After having mapped scenarios of potential conflicts between human rights norms and investment protection norms, the following section will focus on the content of these norms and on uncertainties in the fields of human rights and investment protection with regard to the exact scope of the human rights obligations and investment protection clauses.

3. Lack of Clarity of the Substantive Norms

Clarity about the normative content of both human rights protection norms and investment protection norms is important for the legal security of all actors concerned. A lack of clarity in regard to substantive human rights norms, where neither the investor nor the State knows the exact scope of the

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24 Ibid., para. 42.
25 Ibid., para. 43.
26 Ibid., para. 125.
27 See infra section 3.2. The Unclear Borderline Between Regulatory Takings and Police Powers.
human rights obligations incumbent on the State, causes problems already at the stage of drafting concession contracts in a way to prevent future human rights violations.

An unclear legal situation in the field of investment protection with regard to the legal classification of regulatory measures of States in the post investment phase creates an unsatisfactory situation for both investors and States. Investors are not in a position to correctly assess their investment risk. States do not know the legal consequences of regulatory measures they would wish to undertake.

3.1. The Unclear Scope of Economic, Social & Cultural Rights

From a human rights’ perspective, States have an obligation to respect, protect and fulfill human rights of the population in all contexts thus also with regard to foreign investment and privatization. Hence, when entering into privatization agreements they are under an obligation to make sure that they are able to honour their human rights obligations.

With regard to subsequent treaty obligations the European Commission on Human Rights stated the following:

… it is clear that, if a State contracts treaty obligations and subsequently concludes another international agreement which disables it from performing its obligations under the first treaty, it will be answerable for any resulting breach of its obligations under the earlier treaty.29

The same must of course be true for an agreement under domestic law, which contains an arbitration clause providing for dispute settlement by an international arbitral tribunal.

This has consequences on two levels. The State has to take into consideration its human rights obligations when concluding a BIT as well as when concluding an investment agreement with an investor. To be in a position to do so, it would be useful if not necessary to know the exact content of the human rights to be taken into consideration when entering into investment agreements.

The difficulties which prevail in this regard concerning economic, social and cultural rights have their origin in certain features of the UN Covenant on Economic, Social and Cultural Rights (CESCR).

One reason for the fact that civil and political rights are clearer than economic, social and cultural rights is a political one. Civil and political rights have attracted much more attention from doctrine as well as practice, while economic, social and cultural rights have often been neglected and were

28 See e.g. M. Nowak, Introduction to the International Human Rights Regime, 48 et seq. (2003).
29 European Commission of Human Rights, no. 235/56, Decision, 10 June 1958, Yearbook 2, 256, at 300.
surrounded by controversies of an ideological nature.\textsuperscript{30} Thus for a long time there was a lack of case law as well as of doctrinal analysis with regard to these rights.

Other reasons for the somewhat unclear content of the obligations stemming from economic and social rights are linked to substance. One factor is the formulation of the obligation in Article 2 of the CESCR\textsuperscript{31} another one the fact that the protection and fulfilment of rights often require positive measures. It is always more difficult to know when rights are violated by omission rather than by positive action.

Another complicating factor with respect to economic, social and cultural rights is the fact that State parties have undertaken to take steps to the maximum of their available resources to ‘achieve progressively’ the full realization of the rights in that Covenant. The words ‘achieve progressively’ have often led to misinterpretations. It was assumed that the norms contained in the Covenant are more of a programmatic nature than civil and political rights, which contain immediate obligations for states. The Committee on Economic, Social and Cultural Rights specified in its General Comment No. 3 that there is an obligation to move as expeditiously as possible towards the realization of these rights.\textsuperscript{32} In the subsequently adopted Children’s Rights Convention (CRC)\textsuperscript{33} Article 4, which is concerned with economic, social and cultural rights of children, only refers to the available resources and omits the words ‘achieve progressively’ contained in Article 2 CESCR. Although in the CRC some progress regarding the scope of the obligation has been made, the obligation is still conditional upon available resources. This conditionality still causes uncertainty about the exact extent of the obligation at any given time.

The third factor which leads to a lack of clarity regarding the exact scope of the State parties’ obligations is of a procedural nature. It is linked to the lack of an international mechanism for considering individual complaints on all aspects of economic, social and cultural rights.\textsuperscript{34} As a consequence, an exact delimitation of the concrete obligations of States is still missing. The only

\textsuperscript{31} Art. 2 CESCR:

\begin{quote}
1. Each State Party to the present Covenant undertakes \textit{to take steps}, individually and through international assistance and co-operation, especially economic and technical, \textit{to the maximum of its available resources}, with a view to \textit{achieving progressively} the \textit{full realization} of the rights recognized in this present Covenant by all appropriate means, including particularly the adoption of legislative measures. (Emphasis added.)
\end{quote}

\textsuperscript{34} The Commission on Human Rights established a Working Group to consider options for the
possibility to complain about specific aspects of economic, social and cultural rights exists under the optional protocol to the women’s rights convention and under Article 14 CERD. Thus concrete cases of privatizations cannot be tested with regard to their human rights compatibility unless there is a specific gender or racial discrimination component.

Had there been an individual complaints procedure, the inhabitants of Cochabamba would have been able to find out whether Bolivia had violated their right to access to water by concluding the kind of agreement the government entered into with Aguas del Tunari. This in turn could then have served as a guideline for future cases.

The process of clarification of the normative content of economic social and cultural rights and the corresponding obligations has been slow. Some precision has been obtained by way of ‘general comments’. Using this method, the UN Committee on Economic, Social and Cultural Rights interpreted and clarified the content of the norms of the Covenant on Economic, Social and Cultural Rights.

It would therefore be wrong to state that the content of the right to water, which was at stake in the cases mentioned above, is totally unknown and unclear. The right to water has attracted a lot of attention over the last years and is now referred to as a basic human right. The UN Committee for Economic, Social and Cultural Rights issued a General Comment in 2002 in which it outlines the content of the right to water and the obligations of States in regard to the fulfilment of this right.

Some important aspects of the General Comment with regard to privatization are:

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elaboration of an individual complaints procedure under the ICESCR (Resolution 2003/18, paras. 12, 13).


37 See Eide, supra note 30, at 9.

38 Report of the UN Secretary General, Freshwater management: progress in meeting the goals, targets and commitments of Agenda 21, the Programme for the Further Implementation of Agenda 21, and the Johannesburg Plan of Implementation, E/CN.17/2004/4, at 25, referring to General Comment No. 15 of the United Nations Committee on Economic, Social and Cultural Rights adopted in November 2002, where it is stated that: “the human right to drinking water is fundamental for life and health. Sufficient and safe drinking water is a precondition for the realization of all human rights.” (E/C.12/2002/11).

The human right to water entitles everyone to sufficient, safe, acceptable, physically accessible and affordable water for personal and domestic use. The right is amongst others included in the right to an adequate living standard protected by Article 11, paragraph 1.\footnote{Ibid., para. 2; see also General Comment No. 6, para. 32, contained in document E/1996/22.}

With regard to the normative content of the right to water the Committee specified that it contains both freedoms and entitlements.\footnote{Ibid., para. 10.} Especially valid for the topic under consideration is that the freedoms include the right to access to existing water supplies necessary for the right to water as well as the right to be free from interference. It expressly mentions the right to be free from arbitrary disconnections or contamination of water supplies. The entitlements include the right to a system of water supply and management that provides equality of opportunity for people to enjoy the right of water.\footnote{Ibid., para. 23.}

With regard to privatization issues it states that the State must:

- prevent third parties from interfering in any way with the enjoyment of the right to water or from compromising equal, affordable, and physical access to sufficient, safe and acceptable water;\footnote{Ibid., para. 24.}
- prevent companies based in their territory from violating the right to water in other countries (host countries to investment);\footnote{Ibid., para. 33.}
- prevent arbitrary or unjustified disconnection or exclusion from water services or facilities.\footnote{Ibid., para. 44(a).}

The General Comment furthermore provides for a procedure that has to be followed before any action that interferes with an individual’s right to water may be carried out. The relevant authorities must ensure that such actions are performed in a manner warranted by law and in conformity with the Covenant. There has to be an opportunity for genuine consultation with those affected and there has to be timely and full disclosure of information on the proposed measures and reasonable notice of the proposed actions. Legal recourse and remedies against the measures have to be available. Legal assistance has to be provided for obtaining legal remedies. Where the interference is based on a person’s failure to pay for water, their capacity to pay must be taken into account. Under no circumstances shall an individual be deprived of the minimum essential level of water.\footnote{Ibid., para. 56.}
The General Comment was issued after most disputes, which led to current investment arbitration cases, had arisen. Therefore it is difficult to assess how predictable the by now clarified scope of the right was for the different actors in the investment disputes mentioned above, when they entered into their contractual relationships.

The General Comment has certainly brought some clarification regarding the substantive and procedural requirements with regard to the right to water; however, it cannot fully compensate for the missing case law. Only case law is able to explain the vague formulation typical for human rights norms by outlining through concrete examples the exact obligations contained in a human rights norm.

The immediate addressee of these obligations is of course the State. The Covenant itself is only binding upon States and not upon natural or juridical persons. The State itself is obliged to ensure that third persons do not infringe these rights. It has to achieve this through its legal system and of course also by honouring these obligations when entering into contracts with foreign investors.

As we have seen, this is in line with the case law of the European Court of Human Rights with regard to pollution by private enterprises.48 In this context the Court found that the State is under an obligation to ensure that private companies do not infringe human rights of persons under its jurisdiction.49

Hence, the government or its substructures have to consult the population when a formerly public infrastructure is privatized. It also has to ensure, already in the concession agreement that those who are not in a position to pay the rates charged by the private supplier are taken care of. This can be done in at least two ways. One possibility is to oblige the private supplier to provide free service to households below a certain income. Another possibility would be to provide for a system of State subsidies for such households.

In situations where the State has failed to act in accordance with its obligations when concluding the contract with the foreign investor and later wants to correct this situation by imposing new regulations in this particular field, the foreign investor may be able to challenge its treatment by the State before an international arbitral tribunal.

The investor may use BIT provisions to challenge human rights-inspired regulations that interfere with its investment. Such a situation and the possible role of human rights in investment arbitration will be discussed in the next part of this paper.

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48 See supra section 2. Scenarios of Potential Conflict.
3.2. The Unclear Borderline between Regulatory Takings and Police Powers

After having shown the difficulties which still exist with regard to economic, social and cultural rights regarding the delimitation of the exact obligations of States at given times, the following section focuses on the different approaches chosen by arbitral tribunals with regard to regulatory measures when deciding whether the measures adopted by the State rose to the level of an expropriation.

As already mentioned, legal security regarding the legal consequences of regulatory measures would facilitate decision-making for both States and investors. Investors would know whether they face the risk of their investment being seriously interfered with, without any State obligation to compensate pursuant to regulations that intend to correct a situation, which is problematic from a human rights perspective. The State would be in a position to evaluate the consequences of post investment regulations in the domain of human rights. As will be shown, the current situation with regard to indirect (regulatory) expropriations of foreign investments is highly problematic.

One of the substantive standards traditionally covered by BITs is the prohibition of uncompensated expropriations. Investments may not be subjected to expropriation or measures having an effect equivalent to expropriation except where such expropriation is for a public purpose, not discriminatory, carried out under due process of law and accompanied by the payment of prompt, adequate and effective compensation.\(^{50}\)

Two types of expropriations have to be distinguished: direct and indirect expropriations. The latter includes creeping and regulatory expropriations.

The first category, direct expropriation, causes few problems: a formal transfer of property rights is required and if that is the case, compensation will be due no matter what the cause for the expropriation was.\(^{51}\) The situation is more difficult when it comes to indirect expropriations, especially regulatory takings. In this field a clear conflict of interest arises between the regulatory interests of States and investment protection interests. It is established in international law that not every regulatory interference with property rights is an expropriation and thus has to be compensated. Brownlie stated that:

> State measures, prima facie a lawful exercise of powers of governments, may affect foreign interests considerably without amounting to expropriation. Thus, foreign assets and their use may be subjected to taxation, trade restrictions


\(^{51}\) See e.g. Compañía del Desarrollo de Santa Elena, SA v. Republic of Costa Rica, Award, 17 February 2000, 5 ICSID Reports 153, para. 71.
involving licenses and quotas, or measures of devaluation. While special
facts may alter cases, in principle such measures are not unlawful and do not
constitute expropriation.52

Similarly the Iran US Claims Tribunal (IUSCTR) held in *SEDCO*53 that

> [i]t is also an accepted principle of international law that a State is not liable
> for economic injury which is a consequence of bona fide ‘regulation’ within the
> accepted police power of states.

On the other hand doctrine as well as arbitral decisions support the view that
regulation can amount to expropriations.

In *Pope & Talbot v. Canada*,54 a case concerning soft lumber export quotas
a NAFTA Tribunal stated that

> […] the scope of article 1110 [the norm regulating expropriations] does cover
> nondiscriminatory regulation that might be said to fall within an exercise of a
> state’s so-called police powers.55

A NAFTA Tribunal in *SD Myers v. Canada*,56 a case concerned with a temporary
export prohibition of dangerous waste (PCB - polychlorinated biphenyl), did
not exclude expropriations through regulatory measures when it stated that

> [t]he general body of precedent usually does not treat regulatory action as
> amounting to expropriation. Regulatory conduct by public authorities is
> unlikely to be the subject of legitimate complaint under Article 1110 of the
> NAFTA, although the Tribunal does not rule out that possibility. 57

Two doctrines currently dominate the jurisprudence of international arbitral
tribunals on indirect takings. One has been called ‘sole-effects’ doctrine, the
second one is sometimes referred to as ‘police-powers’ doctrine.58

Under the ‘sole effects’ doctrine the determining factor whether an indirect
expropriation has occurred is solely the effect of the governmental measure on
the investment. The purpose of the governmental measure is without relevance
for the determination whether an expropriation has occurred.

53 SEDCO Inc. v. NIOC, Award, 24 October 1985, 9 IUSCTR 249, at 275.
54 Pope & Talbot v. Canada, Award, 26 June 2000, 7 ICSID Reports 69.
55 Ibid., para. 96.
1408.
57 Ibid., para. 281.
58 R. Dolzer, *Indirect Expropriations: New Developments?*, 11 NYU Environmental Law
Realignments?*, 5 International FORUM de droit international 155-165 (2003); G. C. Christie,
*What Constitutes a Taking of Property under International Law?* 38 British Year Book of
International Law 305, at 310 (1962); W. M. Reisman & R. D. Sloane, *Indirect Expropriation
The ‘police-powers’ doctrine also considers a range of other factors such as the purpose and context of the measure, the character of the measure and the interference in legitimate expectations of the investor. In some cases, almost exclusive importance is attached to the purpose.

A typical example of a case with a privatization background where an arbitral tribunal applied the sole-effects doctrine is the case of Metalclad.59 The claimant had been assured by the Federal Government of Mexico that its project for a hazardous landfill facility was compliant with all relevant environmental and planning regulations. Despite these assurances, the local municipal authorities denied a construction permit. In addition, the regional government declared the land in question a national area for the protection of rare cactus. A NAFTA Tribunal stated:

... expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favor of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be expected economic benefit of property ... 60

By permitting or tolerating the conduct of Guadalcazar in relation to Metalclad ... Mexico must be held to have taken a measure tantamount to expropriation in violation of NAFTA Article 1110(1).61

And it continued:

[the] Tribunal need not decide or consider the motivation or intent of the adoption of the Ecological Decree. Indeed, a finding of expropriation on the basis of the Ecological Decree is not essential to the Tribunal’s finding of a violation of NAFTA Article 1110. However, the Tribunal considers that the implementation of the Ecological Decree would, in and of itself, constitute an act tantamount to expropriation.62

Hence, the Tribunal took only the effects and not the motives of the measures into consideration for deciding whether an expropriation had occurred.

A case with a slightly different approach was Tecmed.63 There the Tribunal attached considerable importance to the effects of the measure undertaken by the state but also took additional aspects into consideration when deciding whether an expropriation had occurred. The case concerned a waste disposal

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59 Metalclad Corp. v. United Mexican States, Award, 30 August 2000, 5 ICSID Reports 226.
60 Ibid., para. 103 (emphasis added).
61 Ibid., para. 104.
62 Ibid., para. 111.
facility. The authorities refused to renew an operating permit for a landfill. The ICSID Tribunal found that this failure constituted an expropriation. It first held that

[under international law, the owner is also deprived of property where the use or enjoyment of benefits related thereto is exacted or interfered with to a similar extent, even where legal ownership over the assets in question is not affected, and so long as the deprivation is not temporary. The government’s intention is less important than the effects of the measures on the owner of the assets or on the benefits arising from such assets affected by the measures; and the form of the deprivation measure is less important than its actual effects.]

After having examined the impact of the measure upon the investment, the Tribunal assessed whether the impact of the interference was proportional to the measure’s stated aim (protection of the environment and public health) and found that this was not the case. Therefore it did not only rely on the impact of the measure but also on its purpose. Hence, it also included human rights considerations in balancing the various interests at stake.

Typical examples for the police powers doctrine are the recently decided cases Methanex and Saluka. Only Saluka occurred in a privatization context, but both represent extreme examples of the police powers doctrine and hence deserve mention here.

Methanex did not arise in a privatization context but still concerned public health and hence human rights. The case arose out of a ban of the gasoline additive MTBE in California. California argued that banning MTBE was necessary because the additive contaminated drinking water supplies, and therefore posed a significant risk to human health and safety, and the environment. The company argued that the ban was tantamount to an expropriation of the company’s investment, a violation of NAFTA’s Article 1110, and was enacted in breach of the national treatment (Article 1102) and minimum international standards of treatment (Article 1105) provisions.

The Tribunal found that the measure was for a public purpose and non discriminatory and no specific commitments had been given to the investor. Therefore, no expropriation had occurred. In that way it used the criteria formerly applied to distinguish an illegal from a legal expropriation to decide whether an expropriation had taken place at all. From the perspective of legal logic such reasoning is not permissible as it uses the conditions for further legal consequences to argue that if they are fulfilled the original premise will

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64 Ibid., para. 116; footnotes omitted.
68 Methanex is a major producer of methanol, a key component in MTBE.
not exist. In other words: according to the Tribunal, if the consequences for a legal expropriation are fulfilled, no expropriation will have taken place. Thus expropriation and regulation would be mutually exclusive unless a specific commitment has been made by the State.

The Tribunal said:

[A]s a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alios, a foreign investor or investment is not deemed expropriatory or compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation.69

Along the same lines the Tribunal in *Saluka v. Czech Republic*70 argued, in the context of the forced administration of a bank, that under customary international law bona fide regulatory measures within the State’s police power do not require compensation no matter how they affect the foreign investor. It said that:

In the opinion of the Tribunal, the principle that a State does not commit an expropriation and is thus not liable to pay compensation to a dispossessed alien investor when it adopts general regulations that are “commonly accepted as within the police power of States” forms part of customary international law today. There is ample case law in support of this proposition. As the tribunal in *Methanex Corp. v. USA* said recently in its final award, “[i]t is a principle of customary international law that, where economic injury results from a bona fide regulation within the police powers of a State, compensation is not required”.71

If this extreme form of the police powers doctrine prevails the regulatory capacity of host States to introduce new measures to promote and protect human rights will be unlimited in the long run. On the other hand this will have disastrous effects on investment protection. The concept of indirect expropriation will lose most of its meaning. The expropriation clauses in BITs, although also referring to indirect expropriations and measures tantamount to expropriation will, in effect, only cover formal or discriminatory expropriations or cases where an explicit commitment has been made. Hence BITs will largely be deprived of their function to protect foreign investors against abuse or disproportional use of police powers by States.

In analysing the two strands of jurisprudence it becomes clear that we have a binary system before us. The tribunals in the tradition of the sole effects doctrine only focus on the effect on the investor to decide whether an expropriation has occurred and are left with an all or nothing solution with

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regard to compensation. The tribunals using a radical police powers doctrine ignore the effects of the measure and instead focus only on its purpose for deciding whether an expropriation occurred. They are left with the same ‘all or nothing’ solution with regard to compensation.

The only case of those mentioned here where a somewhat intermediate approach was chosen, was *Tecmed*. In this case the Tribunal basically relied upon the sole effects doctrine but re-examined its findings taking the purpose of the interference also into account. In doing so it applied a proportionality test. In the end this also led to an all or nothing situation as regards damages since the proportionality test was applied only to find out whether an expropriation existed or not. Once the Tribunal found that an expropriation had occurred, the State had to pay full compensation. Thus, under the current system no matter which strand one favours a real balancing of interests is not possible since the outcome of the analysis is always whether an expropriation has occurred or not. Depending on this finding either full damages have to be paid or none at all. No matter which approach is chosen the outcome is an often dissatisfactory ‘all or nothing’ result. After balancing the various interests at stake a distribution of economic burdens is not possible.

Since it is impossible to predict which strand a tribunal will follow and which outcome it will reach, neither investors nor States are in a position to foresee the consequences of their actions. Investors do not know whether they will have to face interferences in their investment because of human rights considerations whose consequences were not reflected in the investment contract. States, on the other hand, do not know whether they have to face large compensation payments if the result of a regulation to fulfil human rights obligations is a substantial deprivation of the foreign investment. It is of immediate interest, also from a human rights perspective, that this situation of legal uncertainty is brought to an end. One fact complicating the issue is the lack of interfaces between human rights protection mechanisms and investment protection. This will be analyzed in the following section.

Before turning to this important procedural aspect of the problem, some thoughts on a more balanced approach to the issue of expropriation shall be outlined. Such an approach exists in the human rights protection system. The way in which the human rights protection system would balance the property rights of the investor and the right to water of the consumers shall be explained briefly.
In the human rights context the right to property as such is only protected at the regional level. No infrastructure privatization case has so far been decided either by the European or the Inter-American Court of Human Rights.

The protection provision of Article 1 of Protocol I consists of a three-layered system: the scope of application, the norms concerning the interferences and a requirement for justification of the interferences which comprises a proportionality test. Unlike international investment protection, which only protects against uncompensated expropriations, it provides for a gradual concept of interference comprising a catch-all clause. Once an interference has been established, the Court first has to assess whether it was in the public interest and lawful. Then, and this is the important step for the topic under consideration, it undertakes a balancing test whereby it evaluates whether the interference strikes a fair balance between the demands of the general interests of the community and the requirements of the protection of the complainant’s human rights. This balance will not be found if the person concerned has had to bear an individual and excessive burden.

This system, whereby the existence of a reasonable relationship between the goal and the effects of the interference is verified, allows for a balancing between the general interests of the community and the property interests of the investor. In this process, a number of factors such as the amount of compensation paid to the investor and legitimate expectations of the investor can be taken into consideration. Therefore the ‘all or nothing’ approach, typical for international investment law, is replaced in the human rights system by a balancing approach where the proportionality of the measures is the main goal. According to this approach, the first step is to decide whether an interference has occurred. The second step is to analyze whether this interference was proportional. This could serve as an example for international investment protection. Exactly how this could be achieved is the object of another study that is currently work in progress.

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72 Art. 1 of Protocol I to the Convention for the Protection of Human Rights and Fundamental Freedoms; Art. 21 American Convention on Human Rights; Art. 14 African Charter on Human and Peoples’ Rights. Neither the UN Covenant on Civil and Political Rights nor the UN Covenant on Economic Social and Cultural Rights provide for the protection of the right to property as such.

73 Tangible as well as intangible property rights, contract rights as well as good will are protected by the Convention.

74 See e.g. ECHR, Sporrong and Lönnroth v. Sweden, Judgement, 23 September 1982, Series A, no. 52, paras. 69 and 73.
4. The Protection Mechanisms in the Two Fields Lack Interfaces

After this analysis of how balancing within one system can work, the difficult question arises if and how two different branches of international law, which have factual connections, interact. This topic shall be addressed next.

BITs typically do not contain carve outs for human rights nor condition any of the substantive investment rights upon corresponding human rights responsibilities of the investor. International investment law does not contain a set of rules to be applied in case of a conflict between international investment law and non-investment legal obligations such as human rights obligations. There are some cases where tribunals had to decide on conflicting treaty obligations but none concerned a human rights treaty so far. Therefore issues like what happens with the obligation of the State vis-à-vis the investor if fundamental human rights are violated either by the investor itself or if the investor contributes to a host State’s violation of human rights have not been addressed so far by investment arbitration tribunals.

From the perspective of a human rights body human rights obligations will always take priority. The State will be liable for any breach of its obligations under the human rights treaty, no matter whether it first contracted human rights treaty obligations and subsequently concluded another international agreement which disables it from performing its obligations under the first treaty, or whether it first entered into the investment agreement and afterwards ratified the human rights treaty.

4.1. The Difficult Path for the Affected Individuals to Get their Rights Protected

4.1.1. The Absence of an Individual Complaints Procedure with Regard to Economic, Social and Cultural Rights

As already mentioned, the monitoring of economic, social and cultural rights is relatively weak. The CESCR has no individual complaints procedure and the ones available under Article 14 of the Convention on the Elimination of Rational Discrimination (CERD) and CEDAW are only applicable in a discrimination context.

76 European Commission of Human Rights, no. 235/56, Decision, 10 June 1958, Yearbook 2, 256, at 300.
Sometimes it is possible to obtain an efficient protection of economic and social rights via the application of treaties on civil and political rights. This was the case with the right to housing and Article 1 of Protocol 1 of the ECHR in the case of Öner and Ziy structure. As already mentioned, in cases of severe environmental pollution that affect individuals' well-being, Article 8 ECHR was successfully invoked. The Court found violations of the Article in the already mentioned case of Lopéz Ostra v. Spain as well as in the case of Guerra et al. v. Italy which concerned a fertilizer factory emitting toxic substances. The Court said:

… severe environmental pollution may affect individuals’ well-being and prevent them from enjoying their homes in such a way as to affect their private and family life adversely. … The Court holds, therefore, that the respondent State did not fulfil its obligation to secure the applicants’ right to respect for their private and family life, in breach of Article 8 of the Convention. There has consequently been a violation of that provision.

If it is not possible to subsume a case under a civil right and the case has no discriminatory element it will not be possible to obtain individual relief under the current international human rights protection system. Thus the adoption of the long discussed optional protocol to the CESCR seems indispensable for a more effective protection of human rights in the field of privatized formerly public services.

4.1.2. Investors Cannot Be Held Accountable by Individuals for Violations of Human Rights

Non-state actors are not directly bound by international treaties for the protection of human rights. Thus they cannot be held responsible in the complaints procedures existing in the field of international human rights protection. An attempt to solve this problem was the adoption of codes of conduct under

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78 Ibid., para. 136.
79 There the Court ruled that the applicant was definitively deprived of his home, a slum dwelling which was destroyed in the course of a landslide provoked by a methangas explosion of the landfill on which it was situated. The positive obligation under Art. 1 of Protocol No. 1 required the national authorities to take practical steps to avoid the destruction of the applicant’s house.
81 Supra note 79, para. 60.
82 See on this issue e.g. M. Scheinin, Economic and Social Rights as Legal Rights, in Eide, supra note 30, 29-54, at 48-49.
the auspices of various international organizations. Enforcement works essentially through naming and shaming but no institution where an individual can complain against such enterprises has so far been created.

Investment tribunals will not be able to hear direct claims of violations of human rights. They must usually restrict themselves to considering allegations of violations of the instruments over which they have jurisdiction. Thus their competence is limited to the standards provided for in the relevant investment treaty. The Tribunal in *Biloune v. Ghana* has found that it was not even competent to decide on the alleged human rights violations inflicted upon the investor. It said:

> Moreover, contemporary international law recognizes that all individuals, regardless of nationality, are entitled to fundamental human rights ..., which no government may violate. Nevertheless, it does not follow that this Tribunal is competent to pass upon every type of departure from the minimum standard to which foreign nationals are entitled, or that this Tribunal is authorized to deal with allegations of violations of fundamental human rights.

A tribunal would be even less competent to decide on human rights violations of persons affected through the privatization of formerly public services who are not parties in the proceedings.

Thus beside the cases where the supervisory structure in place for civil and political rights can be used by individuals to enforce their rights and those cases which have a discriminatory element, individuals cannot obtain relief by using a human rights protection mechanism. Neither have arbitral tribunals any competence to act on behalf of victims of human rights violations.

One way to inform tribunals about the human rights implication of a case under consideration are *amicus curiae* petitions of civil rights groups and human rights NGOs. This approach was taken in cases concerning the privatization of water distribution and sewage systems. This procedural

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86 The investor asserted arbitrary detention and expulsion of Mr. Biloune by the government. (*ibid.*, at 203).

87 *ibid.*, at 203.

88 See e.g. Aguas Argentinas, *supra* note 13, Order in Response to a Petition for Transparency
mechanism of course cannot provide direct relief for victims of violations of the right to water. It does not put individuals in a position to hold the investors accountable but at least assures that the tribunal deciding on the case between the investor and the State can make a more informed decision. The tribunals deciding about these petitions in granting them explicitly referred to the fact that also human rights considerations arise in the cases before them.\textsuperscript{89} The cases are still pending and no decision on the merits has been taken.

4.2. States Trapped between Violating Human Rights and Investment Protection Treaties

Let us return to the example of the water privatization contract. Imagine a situation where an investor fulfils the obligations of the concession contract and had its tariff rates approved by the governmental authorities. Nevertheless it turns out that a certain number of individuals are unable to afford the necessary quantity of water. The State could either impose another tariff scheme on the investor and thus risk violating the investment protection standards or else violate its human rights obligations.

Another situation already described above refers to privatized waste treatment facilities, which so heavily pollute the environment that they violate the human right to respect the home and private and family life.\textsuperscript{90} The State could either impose the installation of filters, order the closure of the facility and thus risk to violate investment protection guarantees or else, as we have seen, violate its human rights obligations.

Violating their citizens’ human rights could become costly when elections have to be won, whereas violating the investor’s rights could become very expensive when arbitral proceedings are lost. The protection mechanisms for individuals against human rights violations are less of a threat for States since the mechanisms in place are far less effective than the ones in the realm of investment protection, where the amounts of damages awarded are larger and the enforcement mechanisms are much stronger.

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\textsuperscript{90} See supra section 2. Scenarios of Potential Conflict.
5. Concluding Remarks

The examples mentioned above show that there are a number of factual linkages between investment and human rights. The unclear scope of economic, social and cultural rights as well as the uncertain situation with regard to the legal consequences of regulatory measures leads to legal insecurity and in that way contributes to problems at the crossroads between these two fields of international law. As the mechanism dealing with human rights and investment protection lack coordinating mechanisms, it is especially important to develop strategies how human rights violations in this field can be prevented.

‘Trap situations’ like the ones described above could be prevented through carefully negotiated concession contracts where both investors and States are sensitive to the human rights implications of privatization projects and decide on sharing the costs for the fulfilment of the relevant human rights obligations at the outset before any dispute arises. A negotiated allocation of responsibilities for the respect of the human rights involved is an essential factor in this regard.

It should be kept in mind that while services can be subcontracted to a foreign investor, the responsibility for the realization of human rights cannot. It rests with the State. One possibility to ensure the observance of human rights is to use resources from (foreign) investors and privatize services. The advantage of this method to improve the human rights situation will be lost if instead of carefully negotiating the contract the State cancels the contract once the investor has provided the capital and insists on the conditions negotiated in the concession contract.

In the field of investment protection more efforts should be undertaken to develop meaningful ways of sharing costs for the implementation of human rights between investors and home States. A balancing between the investors’ and the host States’ interests that does not lead to all or nothing decisions, as is currently the case, could be helpful.

Furthermore, the adoption of an individual complaints procedure in the field of economic, social and cultural rights would be very helpful. The individuals concerned could better ensure the respect for their human rights. Host States and investors would be able to better assess the human rights obligations connected to a particular investment and provide adequate solutions before the violations occur.