CHAPTER 12

The Role of International Environmental Principles in Investment Treaty Arbitration: Precautionary and Polluter Pays Principles and Partial Compensation

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1 Introduction

High-profile investment disputes over the last decade such as the Sakhalin ii oil and gas project case1 Chevron v. Ecuador2 and Vattenfall v. Germany i3 and ii4 have highlighted the ever-increasing issue of conflict between the protection of foreign investment and the protection of the environment. There are circumstances where host state's environmental measures5 may result in the

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1 The project involved rights that were originally owned by Royal Dutch Shell, Mitsubishi Corporation and Mitsui & Co. In 2005–2006, Russian authorities claimed that Sakhalin ii violated Russian environmental regulations. Amid this controversy, the state gas monopoly (Gazprom) took a 50% plus one share of the operator of the project (Sakhalin Energy) in December 2006.

2 The Chevron and TexPet oil exploration and extraction project in the Amazon region of Ecuador has given rise to a long-standing dispute over alleged environmental and social damage, resulting in two investment arbitration cases (Chevron Corporation and Texaco Petroleum Company v. Ecuador, UNCITRAL, PCA Case No. 34877, Final Award of 31 August 2011; and Chevron Corporation and Texaco Petroleum Corporation v. Ecuador, UNCITRAL, PCA Case No. 2009–23).

3 In 2009, a Swiss energy company challenged environmental restrictions imposed by the City of Hamburg, claiming that they were in violations of the Energy Charter Treaty (ECT). The dispute was settled in 2011 (ICSID, Vattenfall AB and others v. Germany, Award of 11 March 2011, ICSID Case No. ARB/09/6).

4 In 2012, the German government's decision to phase out nuclear energy for the commercial generation of electricity in Germany resulted in an investment treaty arbitration based on the ECT (ICSID, Vattenfall AB and others v. Germany, Decision pursuant to ICSID Arbitration Rule 41(5) of 2 July 2013, ICSID Case No. ARB/12/12).

5 For the purposes of this chapter, the term 'environmental measures' refers generally to host state's domestic regulatory measures that cover environmental issues in general, ranging from ecological conservation to the protection of public health. Broad definitions of the term 'environmental legislation' are incorporated into certain investment treaties, e.g. the
restriction of a foreign investor’s interests and give rise to a dispute between the affected investor and the host state. If the dispute cannot be settled by negotiation, the investor may bring a claim to investment treaty arbitration, arguing that such measures amount to a breach of investment treaty obligations. The case law of investment treaty arbitration confirms the existence of such conflicts – indeed, a number of cases (recent examples include *Glamis v. US*,6 *Clayton/Bilcon v. Canada*,7 *Unglaube v. Costa Rica*,8 *Pac Rim Cayman v. El Salvador*,9 *Renco v. Peru*10 and *Abengoa v. Mexico*11) indicate that investment treaty arbitration has now become an important international forum in which environmental issues are discussed. This chapter addresses this tension, focusing on investor-state arbitration that has dramatically increased in importance for the protection of foreign investment. The need for a proper balance between international environmental norms and investment protection provisions in such ‘environment-investment’ conflicts is indeed widely recognised. Despite consensus on the need for balance, however, the question of how such a balance should be sought has been less explored. Without guidance on how to go about it, it has proven to be difficult for tribunals to incorporate the balancing of these interests in the outcome of the disputes before them.

This chapter addresses the vexing question of how to properly balance the interests of foreign investors against environmental concerns, focusing on the remedy phase of legal disputes. Once the liability of the host state is established, the concern of the parties is how much they may receive or have

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6 *Glamis Gold, Ltd. v. US*, UNCITRAL, Award of 8 June 2009.
9 *ICSID, Pac Rim Cayman LLC v. El Salvador*, ICSID Case No. ARB/09/12.
10 *ICSID, The Renco Group, Inc. v. Peru*, ICSID Case No. UNCT/13/1.
11 *Abengoa v. Mexico*, Award of 18 April 2013, ICSID Case No. ARB(AF)/09/2.