

# COVID-19: will State measures give rise to a new set of investment claims?

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Governments around the world have responded to the COVID-19 pandemic with drastic, and at times divergent, measures that impact both the global economy at a macro level, and businesses in many sectors, at a micro level. Foreign investments are likely to be particularly affected by new restrictions on trade, prices, as well as various relief measures being adopted by governments. While the standards of protection provided to investments of foreign investors under investment treaties have been shaped by decades of treaty negotiation and international arbitral practice, the unprecedented nature of COVID-19 and the measures it has provoked are likely to raise novel issues in investment disputes.

## How are States' response measures impacting investments of foreign investors?

States have adopted a variety of measures to respond to the health and economic crisis caused by COVID-19, many of which impact foreign investors.

- Extraordinary powers to Governments: Some States may seize the opportunity to impose strict unilateral measures. In Hungary, the Parliament has granted Prime Minister Viktor Orbán the power to rule by decree, while in Israel, the government has imposed sweeping surveillance powers without parliamentary oversight. Unfettered powers may result in overbroad measures severely affecting companies operating in the market.
- Price regulation and export restrictions: To ensure supplies remain available, governments have sought to regulate the market for medical and household supplies by imposing a cap on prices and prohibiting exports. The EU has announced restrictions on the export of personal protective equipment, while in Italy, the country's only producer of ventilators has been ordered to reserve all of its production for domestic use. For some companies, this may dramatically decrease sales revenues even for in-demand products.
- Suspension of payments: As a measure of economic relief, both El Salvador and Bolivia have temporarily suspended utility payments for all citizens. Utility companies, many of which are foreign-owned with investor rights, have as a consequence seen their revenue streams eliminated.

- **Compelling production**: States may use emergency powers to compel private companies to produce medical supplies, as the United States has already done, ordering General Motors to produce thousands of ventilators. While laws such as the US Defense Production Act generally require that the government compensate companies for producing materials, they may impose reduced prices or require companies to prefer local clients. The race to develop a vaccine may also revive interest in nationalizing production lines to ensure adequate local supplies.
- **Seizing private property**: In Europe, States have requisitioned private supplies of masks and other protective equipment for use in State-run hospitals, while in China, laws allowed the government to temporarily seize private hotels and hospitals to house patients. The amount of compensation provided for such seizures, if any, has varied significantly between countries.
- **Measures with indirect impacts**: Even when companies are not directly targeted, State-mandated closures and cancellations drastically affect private investments in almost all business sectors. In most European States, all non-essential businesses have been ordered to close until further notice, significantly reducing or entirely eliminating any income during this period. The transportation industry has been one of the first victims of such restrictions. Measures restricting national travels or closing airspaces, for instance, have severely affected bus and train companies and airlines.

Foreign investors, even if not explicitly targeted, may be disproportionately impacted by such measures due to the transnational nature of their businesses, which particularly depend on open borders and unrestricted movement of persons and goods.

### **What legal protections exist for aggrieved investors?**

Many countries have coordinated their response efforts with private industries to implement the above measures voluntarily and amicably. However, States have also resorted to unilateral action to respond to the health crisis, which may encourage foreign investors to seek recourse under protections found in investment treaties between their host States and home States.

Most investment treaties provide for dispute resolution through tribunals constituted under the International Centre for the Settlement of Investment Disputes (“ICSID”) or other arbitration rules. To pursue a claim, aggrieved investors must comply with procedural requirements set out in the relevant treaty, which may require, for example, advance notice and observance of “cooling off” periods before a claim can be filed.

Most arbitral institutions, including ICSID, appear to be quickly adapting to the novel challenges posed by the COVID-19 crisis and actively encourage electronic filings and online hearings to ensure continued operation. Where urgent interim relief is needed, the ICSID Rules, like other arbitration rules, allow tribunals to order provisional measures to preserve the parties’ rights. However, expedited, or “emergency” arbitration is generally unavailable in investment disputes.

The specific protections granted to investments of investors will depend on the exact language of the treaty. In the context of the COVID-19 emergency, the protections that investors are more likely to invoke include fair and equitable treatment, the guarantee of protections equal to those given to national investors, and protection from unlawful expropriation.

- The fair and equitable treatment standard prohibits arbitrary measures reflecting disregard of due process of law or that are unreasonable or excessive considering the circumstances. In evaluating claims, tribunals will generally weigh whether the effects

of the intended measure remain proportionate with regard to the affected rights and interests.

- Under “national treatment” or “most favored nation” clauses, States must treat foreign investors as favorably as local investors, or at least as favorably as foreign investors from other countries. Consequently, State measures that specifically target foreign investors or unreasonably favor the national industry could violate these standards of protection.
- Most treaties require any expropriation to be done with a public purpose, in accordance with due process and to be accompanied by adequate compensation. Government seizures of private property or other acts affecting an investment may give rise to claims of unlawful expropriation, if it not accompanied with adequate compensation.

### **Can States raise COVID-19 as a defense for response measures?**

States may not be able to defend an exercise of unconstrained powers simply by pointing to the global crisis engendered by COVID-19. However, international law gives States broad power to act in emergency situations, and States could invoke a number of doctrines to defend conduct that is narrowly tailored to respond to the crisis.

International arbitral practice recognizes that States may exercise their police powers to legislate in the public interest in a reasonable and non-discriminatory manner. This defense permits States to adopt regulations in good faith and in accordance with due process without violating treaty obligations.

Some investment treaties also contain explicit “exceptions” permitting measures that are necessary for protecting national public policy interests. A minority of treaties categorically state that measures taken out of necessity “shall not be the subject of a claim,” while most impose conditions for a State to invoke such a defense.

Even in the absence of a specific treaty exception, customary international law as codified in the ILC Articles on the Responsibility of States for Internationally Wrongful Acts precludes the wrongfulness of an act of a State in a number of cases.

The defense of necessity excuses States from responsibility when its actions are the only way to safeguard an essential interest from “grave and imminent” peril. This defense, which was invoked (with mixed results) by Argentina in its response to the country’s 2001 debt crisis, could apply equally to actions taken out of medical rather than economic necessity.

A State may also plead that its actions are justified by distress. For this defense to succeed, the State must demonstrate: (i) a threat to life; (ii) a special relationship between the State and the persons whose lives are threatened; (iii) that there was no other reasonable way to deal with the threat; (iv) that the State did not contribute to the threat; and (v) the proportionality of the measures adopted.

Finally, the force majeure defense is perhaps the most limited, as it only excuses a State from obligations where an unforeseeable event beyond the control of the State makes performance of the State’s obligations materially impossible. Force majeure would not generally be a basis for a State to defend affirmative measures that it chose to adopt.

## Conclusion

States have taken very different measures impacting investments within their territory, all of which they will surely claim are necessary and justified. It cannot be denied that these are indeed exceptional times, as investors have also acknowledged. However, the defenses listed above would not necessarily cover every measure a State might take, and there may well be gray areas, linked to the breadth and significance of measures, the timing of their application, and aspects of potential compensation. For States to avoid liability for measures adopted in response to the COVID-19 pandemic, it will likely be crucial to be transparent about the scope and purpose of their measures, to observe applicable local laws and fundamental principles of due process, such as non-retroactivity, as well as to ensure proportionality and that measures do not favor or discriminate against investors based on their nationality. Legitimate claims under investment treaties may well arise, and both States and investors would be well advised to be aware of their rights where such sensitive and difficult issues are concerned.

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