ESG

ANGOLA

ESG and investment treaties in Africa: a new substantive standard?

After ratification of the first sustainable investment facilitation agreement, between the EU and Angola, Carla Gonçalves Borges, Mariana França Gouveia, and Assunção Cristas of Vieira de Almeida analyse ESG considerations in African states' investment treaties

Introduction: today's ESG standards

The foundation of the current ESG framework can be traced back to the Earth Summit held in Rio de Janeiro in 1992, where a coalition formed by political leaders, scientists, and non-governmental organisations sought to develop a global action plan focusing on the impact of human socio-economic activities on the environment.

The principles laid down by the Earth Summit have been pivotal in shaping the current ESG standards. The ESG framework now comprises a robust system of domestic and international laws, regulations, and soft-law instruments that are fundamental to sustainable and ethical business conduct.

Whether driven by legal obligations, reputational concerns, and/or financial benefits, the corporate sector has actively embraced the shift towards sustainability, with companies increasingly integrating ESG criteria into their business models and investment strategies. Their additional concerns include combating climate change (mitigation and adaptation), the safeguarding of the environment, human and labour rights (including within companies' supply chains), and the avoidance of harmful business practices.

The ESG ecosystem has profound implications for international investments in developing and low-income countries, especially in Africa. With abundant natural resources, a need for sustainable development, susceptibility to climate change, and manifold social challenges, this unique and pressing set of circumstances needs to be tackled by local governments, with the support of developed countries and international investors.

The most recent example of this cooperation is the European Parliament's consent to the ratification of the first sustainable investment facilitation agreement (SIFA), between the EU and Angola, which is expected to enter into effect shortly. Angola ranks as the EU's sixth-largest African investment destination, having attracted 7% of the EU's foreign direct investment in the continent with a total of €14.1 billion in 2021.

Within this context, a broader trend can be seen in international policy and treaty making corresponding to the increased adoption by African states of investment treaties with ESG-aligned language (see section 2 below), which could represent a new substantive set of rules governing the rights and obligations of foreign investors (see section 3).

ESG clauses in international investment agreements

Bilateral investment treaties (BITs) and investment chapters included in plurilateral, regional, inter-regional, or, more broadly, multilateral preferential trade agreements are generally accepted as the most important instruments for the international protection of foreign investments. Dating back to 1959, when the first BIT was concluded between Germany and Pakistan before its entry into force in 1962, BITs have been regulating the treatment of foreign investment, providing a series of guarantees and protections for investors of one contracting state on the territory of the other contracting state.

In the 1960s, the highest number of BITs worldwide were signed by African countries, predominantly partnering with developed nations, according to **the United Nations Conference on Trade and Development's database on BITs**. This trend has been consistently upheld, with a steady stream of investment treaties signed over the years, reflecting Africa's enduring commitment to fostering a conducive atmosphere for foreign investment.

Fast forward over half a century, and the landscape of international investment agreements (IIAs) has evolved significantly, with more than 2,800 treaties signed globally as at 2022.

Reflecting contemporary concerns, many investment treaties signed by African states now include ESG-related clauses. These provisions vary widely, from preamble language that frames the importance of ESG factors to jurisdictional clauses that delineate the treaty's applicability to ESG issues. They also encompass substantive obligations that clearly define the ESG duties of the contracting parties, and institutional arrangements empowering designated joint committees to consider and interpret ESG standards.

In October 2023, the ESG Subcommittee of the International Bar Association's Arbitration Committee published a study on "ESG obligations in investment treaties" in its **Report on use of ESG contractual obligations and related disputes**, which examined ESG clauses within investment treaties. Data from the IIAs involving African countries reveals that the earliest text incorporating an ESG clause dates back to 2008. In its model BIT, Ghana not only included ESG principles in its preamble but also stipulated that investors shall comply with the labour, health, and environmental laws and regulations of the host state. The model BIT also presented an environmental carve-out for non-discriminatory measures taken by a host state, which prevents investors from arguing over indirect expropriation of investments affected by such measures.

Following Ghana's lead, countries such as Benin, Nigeria, Senegal, and Morocco have signed BITs or incorporated clauses in their model BIT containing similar substantive ESG obligations.

Despite their varied wording, these substantive clauses consistently convey three key points:

- Foreign investment should not be encouraged through the relaxation of domestic health, safety, or environmental measures;
- Investors are encouraged to voluntarily embrace internationally recognised corporate social responsibility standards that encompass labour, environmental, human rights, community relations, and anti-corruption practices; and
- States maintain their autonomy to regulate ESG-related matters, which effectively exempts certain state actions from triggering the state's investment protection duties under the treaty.

This last exception typically includes caveats, stipulating that the state's measures must be necessary and non-arbitrary.

The Nigeria–Morocco BIT, signed in 2016 but not yet in force, is an example of a treaty containing stringent operational ESG standards for investments. These include the establishment of an environmental management system, adherence to human rights in the host state, compliance with core International Labour Organization standards, and, in some cases, a requirement to obtain certification equivalent to **ISO 14001**.

The treaty also aims to prevent investors from circumventing international environmental, labour, and human rights obligations.

Notably, the Moroccan model BIT, adopted in 2019, not only enshrines these ESG obligations but also introduces a requirement for foreign investors who wish to resolve their investment disputes through arbitration: the treaty bars investors from bringing investment claims if it is found that the investment was made through some form of corruption.

Lastly, **the pioneering SIFA ratified in March 2024 between the EU and Angola** sets out a framework for sustainable investment and mutual development between the parties, encompassing:

- A commitment to uphold environmental and labour laws and standards, without diluting, derogating from, or waiving them with the purpose of attracting foreign investment;
- A commitment to the effective enforcement of international labour and environmental treaties, including **the Paris Agreement**;
- The promotion of corporate social responsibility and responsible business practices; and
- The strengthening of bilateral cooperation on investment-related aspects of climate change and gender equality.

While the SIFA explicitly indicates that it neither creates nor modifies rules on the protection of established investors in the territories of the parties, or of their investments, or on investor–state dispute settlement (ISDS), its implementation is expected to streamline the process for attracting and expanding sustainable investments in Angola by facilitating the establishment and day-to-day operation of businesses for European investors.

Investors and ESG clauses: a new substantive standard?

The ISDS has faced a legitimacy crisis almost since its advent. The fact that it empowers investors to claim compensation from host states for measures taken under the mandate given by their citizens has always led to questions regarding the degree to which arbitral tribunals may exercise the power to overrule a country's electoral choices. Notwithstanding, the inclusion of ESG standards and principles may contribute to a better definition of the limits to the arbitral tribunals' adjudicatory powers.

It is commonly accepted that the inclusion of ESG standards applicable to investments may function as a reinforcement of the host state's right to regulate (see Section 423 of the ruling in ***ADC Affiliate Limited and ADC & ADMC Management Limited v Hungary***, International Centre for Settlement of Investment Disputes, October 2 2006). As stated above, the standards may call for compliance with certain values or rules, or determine the host state's freedom to establish stringent ESG-related standards.

From the perspective of international investment law, a state's right to regulate is particularly relevant to determine the level of protection against regulatory measures granted to an investment. Indeed, the way the host state's right to regulate has been presented in case law and legal doctrine is as follows:

- There is a recognition that it informs and limits the circumstances in which a given host state may act detrimentally in relation to a given investment by approving laws and regulations;
- An exclusion of its liability under the relevant investment treaty, or under a given substantive protection or guarantee;
- As long as no stabilisation clause is in place.

Moreover, the host state's right to regulate has evolved from being understood as a circumstance precluding wrongfulness, subject to certain criteria, to a proportionality assessment that may lead to the exclusion of a duty to compensate the investor.

However, the question is whether the somewhat recent preponderance of ESG standards in international investments can give rise not only to the enhancement of host states' right to regulate, but also be considered as a new substantive standard.

It is possible for ESG clauses and standards to be used by investors to sue host states for action or compensation should any failure to comply with ESG standards affect their investments (see, for example, ***Peter A. Allard v Barbados***, Permanent Court of Arbitration, June 27 2016). However, such cases are arguably less probable than cases where non-compliance by investors with those standards may be used as a defence by host states.

Indeed, it has been suggested (see **ISDS and ESG: Friends or Foes?**) that the inclusion of ESG standards in IIAs may be used as a defence by host states against investors. The protection afforded by these standards stems from the fact that they would limit the host states' consent to arbitrate, thus restricting the cases where its liability to arbitrate with investors would lie. The limitation on the host states' consent to arbitrate would derive from a more nuanced definition of 'investment', which would not only include the general requirements of 'investment' but also the need to comply with the ESG standards.

Although this understanding is still untested in arbitration tribunals, the limitation of a host state's consent due to the investor's failure to comply with the host state's internal laws is not unheard of. Indeed, in ***Worley International Services Inc v Ecuador*** (Permanent Court of Arbitration, December 22 2023), the tribunal stated that the jurisdictional question it was asked to decide on was whether "a State would have given its consent to arbitration to protect investments that breached its own law". When deliberating on this, and bearing in mind that there was no specific provision to that effect, the tribunal asserted that "the absence of an express legality clause in the Treaty does not preclude an enquiry into whether the Claimant's alleged investment complied with the law" (Section 307).

Ultimately, the Tribunal concluded that the state would not consent to arbitration to protect investments that breached its own law (Section 304) and, on that basis, the tribunal declined jurisdiction over the investor's claims, citing "a widespread pattern of illegality and bad faith" in the making of the investment (Section 419).

Moreover, the final award in *Álvarez y Marín Corporation and others v. Panama* (International Centre for Settlement of Investment Disputes, October 12 2018) similarly stated that "In [ISDS], it is reasonable to assume that states have only consented to this curtailment of their sovereignty on the condition that the protective mechanism is limited to investments made in compliance with their own legal system – but does not cover non-compliant investments. To argue otherwise, and to extend coverage to investments made in violation of national law, would go against one of the most basic principles of any legal system: *nemo auditur propriam turpitudinem allegans*" [no one can benefit from their own wrongdoing].

The fact that the claimant was non-compliant with Panamanian law led the tribunal to decline jurisdiction, as the host state's consent to arbitration was implicitly limited to the investor being compliant with said law.

Although, as argued elsewhere (see **2023 in Review: Climate Change and ISDS – Reshaping Investment Arbitration to Achieve Climate Goals**), investment tribunals should uphold international environmental legal obligations. A case where an investor sues a host state as a result of its lack of commitment to ESG obligations is far less probable than situations in which ESG standards are used by host states as a defence against non-compliant investors. In that sense, only time will tell whether there will be a new substantive protection for ESG standards.

Final thoughts on the ESG landscape

ESG is shaping the legal landscape and the ISDS is not immune to this influence. Indeed, in recent years, the inclusion of ESG standards in IIAs has raised the requirements that investors and host states will have to fulfil in investments.

These developments give rise to the question of whether ESG will eventually evolve into a new substantive protection under international investment law. This question arises from the fact that ESG standards can be used by investors to sue host states if compliance with such standards under the relevant IIA is not met. However, although that is possible, the potential of host states relying on such standards for protection against an investor's claims seems more probable.

The widespread and increasing acceptance of ESG standards as binding provisions in IIAs can be widely considered to be a reinforcement of the host state's right to regulate. Indeed, by implementing ESG standards in IIAs, host states are not just adhering to modern treaty making, they are effectively establishing enforceable obligations that investors must comply with if they wish to conduct business in their territory.

Ultimately, by adopting these standards and steering investments towards sustainable, responsible practices, host states may be successful in balancing investor rights with environmental protection and social equity concerns.

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