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COVID-19 and Investment Treaties: Balancing the Protection of Public Health and Economic Interests

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DAY

COMMENTARY  
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## COVID-19 and Investment Treaties: Balancing the Protection of Public Health and Economic Interests

### IN SHORT

**The Situation:** Governments around the world are taking extraordinary measures to address the spread of COVID-19. Although many governments are attempting to strike a balance between the protection of public health and economic interests, the pandemic is creating unprecedented risks for foreign investors around the globe.

**The Result:** Investment tribunals recognise and respect the exercise of significant discretion by States in response to public health issues. However, sovereign measures in response to COVID-19 may violate foreign investment protections contained in international investment agreements ("IIAs") if they are discriminatory or disproportionate.

**Looking Ahead:** Investors should ensure that they have restructured their foreign investments to afford maximum IIA protection in the event of improper State conduct.

The rapid spread of COVID-19, increasingly stringent government orders in response and profound effects on the global economy have raised concerns among corporate directors about how to adequately discharge their fiduciary duties. This *Commentary* is a tool for directors to help them identify some of the benefits that IIAs can provide as they guide their companies during these challenging times.

### The Impact of COVID-19 on Foreign Investment

To curb the spread of COVID-19, States have adopted unprecedented restrictions. Governments have rushed to impose quarantines, travel bans, additional visa requirements and export restrictions. Many States have closed all non-essential businesses and some have nationalised private businesses. China has issued *force majeure* certificates to a record number of local exporters so as to exempt them from fulfilling contractual agreements with overseas buyers. Several influential economies have also passed emergency reforms of their foreign investment review frameworks to allow governments more leeway to block deals or impose conditions on their completion.

In enacting these measures, States are generally attempting to balance competing economic and public health interests. Much of the disruption may be proportionate to the global health risk. However, measures that are taken for overtly protectionist reasons or that otherwise lack credible public interest justifications may constitute violations of foreign investor rights under IIAs. General counsel and board members should bear in mind the protections that may be afforded to their companies by IIAs in the current global crisis.

Given the heightened political, legal and regulatory risks for all  
manner of businesses, investors are advised to review the  
status of their foreign investments under IIAs as a matter of



priority.

### The Protections Provided by IIAs

There are more than 3,000 IIAs in force that provide legal protection to foreign investments. IIAs offer broad legal protections that may not be available under the local law of the host country, and that can supplement the investor's rights under any contracts governing the investment. IIAs generally provide that foreign investors are entitled to be treated as favourably as their local competitors and other foreign investors; establish clear limits on the expropriation of investments and entitle foreign investors to seek compensation; and include additional broad guarantees of treatment for investors in accordance with international law.

To enforce these substantive legal protections, most IIAs provide for investor-state dispute settlement ("ISDS"). This allows investors to initiate international arbitration proceedings against the host State of the investment in the event of a dispute. The ISDS mechanism provides an investor with access to an independent and international tribunal of arbitrators to adjudicate the dispute. These tribunals have the authority to issue final and binding awards that settle the dispute between the parties.

The most potent feature of investor-state arbitration is the international enforceability of the final award against sovereign States. While most States comply with awards voluntarily, awards can be enforced in more than 150 countries under the ICSID or New York Conventions. Often the mere threat of an investment treaty claim against a State can therefore serve as a powerful tool in the hands of foreign investors.

### The Potential for IIA Claims Arising out of COVID-19

Investment tribunals generally pay great deference to governmental judgments in matters such as the protection of public health. However, the proper degree of deference requires a minimum level of rationality and proportionality between the State's measure and a legitimate governmental objective.

States may run afoul of their IIA obligations in a myriad of ways, and each case is evaluated on a case by case basis. In the particular context of COVID-19, measures that are likely to come under challenge from investors include: (i) the denial of nondiscriminatory access to government financial support; and (ii) health-, trade-, or finance-related emergency interventions and measures.

For example, an investor may find that a measure taken in response to COVID-19, such as temporary control over its factory, was disproportionate in the circumstances and gave insufficient weight to the investor's private commercial interests. The nationalisation of businesses for overtly protectionist reasons or without adequate compensation may also have consequences under international law. Further, the denial of market access, for example export restrictions on medical-grade masks or pharmaceuticals, or the suspension of payments due under mortgages or other loans may also contradict IIA protections. So too if States pass legislation mandating that existing insurance contracts retroactively cover COVID-19 cases, particularly if the extent of the impairment is disproportionate to the public purpose. Finally, the administration of State aid or rescue loans may also affect obligations under IIAs, such as protections against discrimination on the basis of nationality or the State's obligations of transparency and protection of investors' legitimate expectations.

Respondent States are likely to contest any IIA claims arising out of the COVID-19 pandemic. In determining whether a measure is reasonable or proportionate, investment tribunals will afford the State a significant margin of appreciation. Moreover, IIAs sometimes contain specific carve-outs that may be triggered by the event of an epidemic or where public health is the object of regulation. States might also seek to rely on customary international law defences such as *force majeure*, distress, necessity or the so-called police powers doctrine to justify the nonperformance of their international commitments. The last of these defences was applied during a smallpox epidemic in the late 19th century. In the *Bischoff Case* (1903), a Mixed Claims Commission found that the seizure of a German carriage by Venezuelan authorities after it had carried two persons infected with the disease did not constitute a wrongful taking under international law.

## Protecting Your Investment Before it is too Late

Well-advised investors should prepare against government overreach by structuring their investments in ways that maximise their protections under an IIA. Just as a company may decide to operate through a subsidiary for tax or other reasons, investment treaty "planning" is often employed by multinational companies in structuring (or restructuring) investments to take advantage of protections afforded by a bilateral or multilateral investment treaty, and investment treaty tribunals have acknowledged and approved that type of planning.

However, investors should pay particular attention to the timing of the restructuring. A number of arbitral tribunals have concluded that investors cannot restructure their investments with the sole purpose of benefiting from IIA protection once the disputed conduct has already occurred. Given the heightened political, legal and regulatory risks for all manner of businesses, investors are advised to review the status of their foreign investments under IIAs as a matter of priority.

### TWO KEY TAKEAWAYS

1. Foreign investors must protect their investments against improper State interference in this time of crisis. Investors should carefully consider how their investments are structured and whether there is scope to restructure their investments in ways that maximise their protections under an IIA.
2. Investment tribunals generally afford significant discretion when adjudicating the legality of State measures in the pursuit of public health goals. However, government measures that are unreasonable, disproportionate, arbitrary or discriminatory may trigger valid treaty claims. General counsel and board members are encouraged to consult with experienced ISDS counsel to ascertain their rights.



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