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**Article**

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## ACCOUNTING, CORPORATE GOVERNANCE & BUSINESS ETHICS | RESEARCH ARTICLE

# Global pandemics and moratorium of investment claims: A perspective from Indonesia

Yetty Komalasari Dewi<sup>1\*</sup>

**Abstract:** The outbreak of the Corona Virus Disease 2019 (COVID-19) has given rise to the intersection of foreign investment protection in connection with adverse regulatory changes and the right of host states to regulate the public interest. Countries have enacted a multitude of policies in pursuit of public health and in handling the repercussions of the pandemic including losses to foreign investors, thus giving rise to arbitral claims. In response, governments may impose customary law defense through the doctrine of police powers under the banner of health reasons. This article features an analysis of Indonesia as a sample country to illustrate possible claims that could arise from its regulatory responses to COVID-19 and possible protections that it can rely upon. In recalibrating the investor-State dispute settlement system, a moratorium on investment claims arising from the pandemic should be endorsed as part of a wider set of reforms.

**Subjects:** Business & Company Law; Regulation; Commercial Law; Sustainable Development; Development Policy; Economics and Development

**Keywords:** COVID-19; investment arbitration; Indonesia; ISDS; moratorium



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Yetty Komalasari Dewi is an Associate Professor and the Head of the Department of Economic Activities and Technology of the Faculty of Law, Universitas Indonesia. She also leads the Legal Center for International Trade and Investment (LCITI), a university research center that engages in research on international trade and investment law. In reviewing developments in these areas of law, LCITI focuses mainly on Indonesia and the Asia-Pacific region, with contemporary topics such as the rise of regional trade agreements and investor-State dispute settlement reform as notable examples of the center's research projects. The COVID-19 pandemic relates to the center's projects on international investment law, specifically with respect to its active monitoring on issues related to international investment as a partner of the Government of Indonesia. Through this research, the center is able to conduct a thorough review of the investor-State dispute settlement from the lens of epidemiology, a new area of research which the center believes would aid in the promotion of international investment law both domestically and in the international stage.

### PUBLIC INTEREST STATEMENT

The onset of the COVID-19 pandemic has forced governments to react promptly by introducing measures to address public health concerns. While such steps are aimed at reducing the spread of COVID-19, they bring forth unintended consequences for foreign investors, whose investments may be negatively impacted because of the government measures in place. Under international investment law, a foreign investor has the legal standing to lodge arbitration claims, which if successful could result in the Respondent state's payment of damages to the claimant investor. The interaction of international health law and international investment law remains a relatively new area of research. More specifically, how host States could overcome the challenge of enacting measures to protect public health while defending against arbitration claims by foreign investors prompts the question of whether reforms should be made to sufficiently address both concerns altogether.

## 1. Introduction

In light of the Corona Virus Disease 2019 (COVID-19) pandemic, countries are challenged to attain a balance between the national economy and public health. Countries may enact governmental measures that hurt the continuance of businesses, including those conducted by foreign investors.<sup>1</sup> Concerning this phenomenon, investors are capable of being subject to domestic regulation that harms their interests, which includes but is not limited to nationalization, requisition, or actions that cause investor businesses to cease operations.<sup>2</sup> Consequently, countries face an ever-escalating risk of investor-State disputes. On the other hand, investors may need to confront the business risk unfolding in the form of newly introduced COVID-19 health and non-health-related regulatory measures. These may include the suspension of contractual rights, social distancing regulations, as well as export and travel restrictions. Health and finance-related measures by states can be challenging to investors, including measures taken during an extreme national emergency. As a response to the pandemic, states are under extreme pressure to enact regulatory measures to contain the impact of the virus on their citizens' health, whether it be through restricting essential medical supplies, enacting social distancing, and quarantine measures, or imposing border and travel restrictions. Host states would raise their sovereign right to enact such regulations based on public purpose. However, it should be taken into consideration that recently, investors have contemplated claims against states in the wake of the pandemic, ranging from changes in national electricity grid regulations in Mexico,<sup>3</sup> to suspension of the collection of tolls by highway concessionaires in Peru.<sup>4</sup> These illustrations present a harrowing risk that enacting policies in response to the pandemic are susceptible to investor claims. This research aims to answer the following research questions. Firstly, it seeks to measure the risk of investor-State claims which may arise as a result of the COVID-19 pandemic. Secondly, it intends to analyze whether host states could adequately defend against investor claims by using existing international law. Thirdly, it proposes the imposition of a moratorium of investor-State arbitration claims as a spearheading solution that would recalibrate the investor-State dispute settlement architecture while allowing reforms to take place accordingly. Traditional defenses in investor-State dispute settlement have been limited to events apart from global health problems such as the COVID-19 pandemic. This study deals with comparing the efficacy of the existing defenses that host States may use to defend against investor claims. The main substantive theory posits that arbitral tribunals would be obliged to take into account the defenses that host States may submit in justifying their government measures. Given the ongoing COVID-19 pandemic and the perceived increased risk of investment arbitration claims against host States, the study assumes that host States would benefit from postponing the resolution of arbitral claims to a later stage in its analysis of the proposed solution of a moratorium of investor-State claims. This study intends to be the first of its kind to extensively discuss the possibility of a moratorium on investor-State arbitration claims, using the COVID-19 pandemic as the basis for a temporary preclusion of claims by foreign investors. By doing so, the study would also be the first of its kind that relates the moratorium to wider investor-State dispute settlement reform options, by presenting it as a joint solution towards amending the investor-State dispute settlement architecture. Hence, the study adopts a balanced analysis, by combining both theoretical and practical authorities by posing real scenarios drawn from examples of government measures and foreign investors' responses to such measures. The study seeks to address current legal questions by juxtaposing them in the intersection between government public health measures and investment protection concerns.

The literature on investment defenses during COVID-19 remains limited so far. Existing literature discussing the implementation of host State measures towards COVID-19 lack a thorough analysis of defenses that host States may rely upon, as they review isolated individual defenses such as security exceptions<sup>5</sup> and police powers,<sup>6</sup> without providing the complete analysis that the current study does. Although some studies provide a more comprehensive analysis of the available defenses, they do not feature the proposed moratorium as does this study.<sup>7</sup> Those that oppose the proposed moratorium do not provide strong arguments against it by discounting the amount of resources host States require to defend against investor claims, while proposing an appropriate standard of review for arbitrators—a reform option that should instead be complemented by the

currently proposed moratorium.<sup>8</sup> Lastly, those that do discuss proposals similar to the moratorium do not go in-depth as to how host States could collectively address the investor claims effectively, on both substantive and technical fronts.<sup>9</sup> Consequently, the current paper seeks to make the following contributions to the existing literature. Firstly, it seeks to prove that investor arbitration claims may arise due to the host states' responses to the pandemic. Subsequently, it presents the case study of Indonesia, a country that is actively reforming its investor-State dispute settlement framework, to highlight the extent to which host States can rely upon both defenses under customary international law and treaties in defending against such investor claims, in reflecting wider regional trends amongst developing countries in the Global South. Indonesia is an emerging economy with active participation in the investor-State dispute settlement sphere as a member of the UNCITRAL Working Group III on ISDS reform. Notably, it is one of several countries that have terminated investment treaties based on a review amidst a surge of ISDS cases in the 2010s. Internally, it is currently developing a new model of investment treaties, which will inevitably factor in recent developments, such as the COVID-19 pandemic. A careful risk assessment on the impact of COVID-19 on investment arbitration and how that would impact Indonesia would not only serve as a guiding policy for the government of Indonesia to draft its upcoming investment treaties, but it would also reflect wider regional trends that may soon culminate, especially as the pandemic remains a current issue that has not yet been resolved. Therefore, if the proposed moratorium were to be enacted as part of a wider set of reforms, Indonesia would be a strategic country to introduce such reforms at an opportune moment. Most importantly, the paper seeks to extensively discuss the proposed moratorium by prescribing both the time frame and mechanism to enact the moratorium, to present a solution that would complement the wider set of investor-State dispute settlement reform efforts.

This paper surveys the existing literature on international investment law by conducting a systematic literature review of sources on both international investment law and health law published from the onset of the pandemic in 2020 to 2022. This review will consist of a comparative and statutory approach to evaluating the circumstances and reasoning of arbitral jurisprudence and contemporary developments in the investor-State dispute settlement sphere. By conducting the review, a thorough understanding will be obtained of the pivotal issues to consider before emphasizing the hypothesis for the requirement of a moratorium to be put in place for investor-State claims. These issues include the potential for investor-State claims, the right to regulate and police powers doctrine, the impact of government measures on investors, legitimate expectations, and the proportionality analysis amidst a global health emergency. Scholars have explored the possibility of raising investor-state disputes. Mao-Wei argues that governmental measures may obstruct the legitimate expectations of foreign investors, as well as possibly violate the promulgated provisions of fair and equitable treatment within the multilateral investment agreement.<sup>10</sup> Nikiema and Nyaguthii also acknowledge the possibility of public health measures in the realms of health, trade, and finance, being challenged by foreign investors. Although possible, Chaisse categorized the pandemic as a state of emergency, arguing that the pandemic requires immediate governmental measures.<sup>11</sup> On the other hand, many scholars have explored states' ability to fight such arbitral claims. Al Dosari argued that the doctrines of force majeure, distress, and necessity under the protection of public health may be sufficient in defending against ISDS claims. However, García noted that the customary law defenses against COVID-19 investment claims may be ineffective, especially since force majeure and necessity requires a high threshold, and distress is still ambiguous upon its applicability within the circumstances of COVID-19. Additionally, Voon noted that issuing for State defense is particularly challenging due to the uncertainty surrounding the standard of review and burden of proof in defending health measures.<sup>12</sup> Ultimately, for an event to be classified as a force majeure event, it must be beyond the control of the party, that the performance of the obligation is materially impossible, and the force majeure situation must not be caused by the state in question. Therefore, while States may claim COVID-19 as a force majeure event, it is unlikely that arbitral tribunals would accept such a defense due to the high threshold in satisfying the elements of force majeure, especially the standard for material impossibility as the mere impediment to performing the act would not

typically fulfill the threshold.<sup>13</sup> Another key discussion arises on the possibility of invoking the police power doctrine. In line with this, Ranjan argued that in the study of India, the government may depend on such doctrine based on the context of arbitral discretion in proportionality and excessiveness.<sup>14</sup> Though these authors all touch on the susceptibility of claims and the defenses that States might use towards resisting them, they do not delve into the core of the issue itself, which is the crucial time whereby States are faced with domestic health crises and impending investor claims. Such a perspective would relate to the possibility of a joint effort by states to propose a comprehensive mechanism geared towards the possible halt of claims that arise from the COVID-19 pandemic.

Given the limited circumstances in which states can defend themselves and the restrictive regulatory space that they are afforded under the current substantive protections in investment protection regimes, there should be a mechanism in place to shield states from the investor claims they stand to face in light of regulatory adjustments they make towards protecting their citizens. Otherwise, investment tribunals make judgments focusing on the extent of the impact of foreign investments rather than highlighting the justifications states may have for their regulatory measures. In mitigating the failure of State defense, significant development has been made by academia, in the form of joint actions to alleviate this burden from states. On 6 May 2020, the Columbia Center on Sustainable Investment (CCSI) led an initiative in the form of a call, signed by advocates of human rights and sustainable development, for an “*immediate and complete moratorium*” on investor-State arbitration claims based on international investment agreements (IIAs) by foreign investors until the resolution of the COVID-19 pandemic, with the restriction extending to all arbitration claims related to government regulations on health, economic and social aspects of the pandemic and its aftermath.<sup>15</sup> This potential reform presents an opportunity for states to be able to realign their priorities to focus on their pandemic relief efforts rather than having to allocate precious resources amid more urgent public health concerns, toward defending investor claims. Particularly in developing countries such as Indonesia, which have limited financial capabilities, namely fiscal constraints in addressing the pandemic, to begin with, there is a heightened sense of urgency to reallocate funds towards the alleviation of the effect of the pandemic on their economies. In consideration of the fact that developing countries form the majority of host states which face investor claims,<sup>16</sup> a moratorium on investor claims can cater to the compelling circumstances that respondent states currently face. While the aforementioned idea has been initiated by CCSI, scholars have yet to explore the necessity and feasibility of such a moratorium during COVID-19.

The purpose of this paper is to explore the propriety of enacting a moratorium during COVID-19, by emphasizing the vulnerability of countries towards the risk of COVID-19-related investor-state claims, whilst focusing on Indonesia. As a net recipient of foreign direct investment and as a party to numerous IIAs, Indonesia has had extensive experience in dealing with investor claims. This experience has resulted in numerous cases that have contributed to the academic discourse in ISDS, which makes the country an ideal example in illustrating the urgency of the proposed moratorium in light of its susceptibility to investment claims.<sup>17</sup> The paper argues that while the right to regulate and the police power doctrine are acknowledged, the existing risk of investor-state dispute is still prevalent due to the enactment of IIAs ensuring legitimate expectations as well as fair and equitable treatment. Due to the likelihood associated with claiming against COVID-19-related measures, the ideal normative defense mechanism is to enact a moratorium to safeguard the interest of both the State and the investor.

This paper starts by elaborating on the grounds for foreign investors to bring claims against the State regarding regulatory measures aimed at COVID-19, which encompasses past trends of investment disputes in times of pandemic and the potential for Indonesian regulatory measures to be the subject of investment claims (section 2). In countering the claims of the investors, the State may assert its right to regulate the police powers doctrine, in which the paper will explore whether the doctrine is prevalent within Indonesian BITs (section 3). Discussions on the police



power doctrine will be complemented by the understanding of its threshold and the context of investment disputes during the COVID-19 pandemic. On this issue, there is a need to consider domestic and international law obligations for investment treaties to determine whether or not the state's action constitutes a justifiable response to the COVID-19 pandemic. Following these essential preliminary clarifications, this article addresses its main goal: to analyze the ISDS-proposed moratorium as a solution to prevent the abuse of claims (section 4). Regarding this, the paper aims to conclude whether the moratorium can be beneficial to both the investor and the State.

## 2. Possible investor-State claims

Amidst the sudden and drastic regulatory changes, one thing remains constant, which is the lingering threat of states' violations of legitimate expectations. Investors often establish their investments after an incentive given by the government of the host state, which need not be explicitly established but accorded to comply with the fair and equitable treatment obligation in treaty provisions states have entered into.<sup>18</sup> To illustrate this, the case of *Copper Mesa v. Ecuador* signifies that the presence of a general exceptions clause was not sufficient in Ecuador's defense of an overhaul of its mining regulations to protect public health and the environment, owing to the high threshold that the clause prescribes.<sup>19</sup> Taken from a host State's point of view, *Copper Mesa v. Ecuador* further calls into question the availability of adequate defense that it may raise when confronted with conflicting objectives to fulfill.

## 3. Investment claim threats arising from COVID-19 related measures

For a relevant illustration, the Mexican government's recent policy approach toward the electricity sector provides an insight into how investor claims might arise from sudden regulatory changes made in light of the COVID-19 pandemic. These changes are part of a series of regulations that have impacted electricity producers involved in wind and solar power generation. In 2019, the Mexican Energy Ministry (SENER) implemented new guidelines, which essentially altered the issuance of clean energy certificates to power plants pre-dating 2014, from the initial framework which only granted the certificates to renewable power plants erected after 2014. Consequently, these guidelines potentially oversaturate the market and thus risk placing downward pressure on the price of renewable energy. Shortly after its implementation, there were already reports on investors anticipating the utilization of investment treaties as a defense against these sudden regulatory changes in the Mexican energy sector.<sup>20</sup> Less than a year after the introduction of these guidelines, the National Center for Energy Control of Mexico (CENACE) implemented a Resolution to Guarantee the Efficiency, Quality, Reliability, Continuity, and Stability of the National Electric Grid of Mexico (CENACE Resolution) during the COVID-19 pandemic.<sup>21</sup> This resolution introduced temporary technical and operational measures, supposedly to alleviate the pandemic's impact on the Mexican National Electricity Grid. Shortly thereafter, the Mexican Ministry of Energy enacted the Resolution for the promulgation of the Policy on Reliability, Stability, Continuity, and Quality in the National Electric Grid (SENER Policy). This policy features a policy statement and a revamp of regulatory measures targeted to alter the Mexican power sector in a manner that favors conventional energy sources for electricity production, predominantly provided by the Federal Energy Commission, while simultaneously overlooking wind and solar power plants. The resolution and policy were later enjoined.<sup>22</sup> Relating to the SENER Policy's temporary enjoinder, while it may serve as a relief for wind and solar power investors, they have renewed their intention to seek domestic legal remedies, along with those provided under existing trade and international agreements.<sup>23</sup> These statements have evolved into consultations with relevant advisory and law firms on the possibility of bringing the disputes to investment arbitration.<sup>24</sup> In February 2021, a Mexican business lobby raised more warnings on treaty claims over the proposed bill with legal experts predicting that such potential claims could be based on national treatment standards found in treaties.<sup>25</sup> The series of seemingly unpredictable regulatory changes in the energy sector may constitute grounds for indirect expropriation provided that the prices agreed by independent power producers plunge to a level that is no longer profitable for the investors.

Previous ICSID cases have shown that the Spanish energy tribunals have ruled in favor of investors' claims for breach of fair and equitable treatment absent a stabilization clause, noting that assurances giving rise to legitimate expectations need not be explicit, which in turn exposes states to a similar level of vulnerability whenever their regulatory changes are deemed as being too much of a radical departure from the legitimate expectations they have set for investors.<sup>26</sup> While the sudden change in regulations in the example of the Mexican electricity sector might not directly result in investor claims, such a threat has proven enough to elevate the sense of willingness that investors are prepared to take in launching one against the State should they feel that the regulations pose an adverse influence on their investments. Other states should take precautions in enacting regulations with the appropriate legal and regulatory processes in their effort to alleviate the impact of the COVID-19 pandemic. These precautions include providing legal certainty to investors to avoid any allegations of violations of fair and equitable treatment, or even indirect expropriation in an investor claim, should they be presented with one.

#### **4. Realized investment claims arising from COVID-19 related measures**

As the aviation and travel industry becomes one of the hardest-hit sectors from the fallout of the COVID-19 pandemic, airport operations are becoming investments with dwindling returns. Chile has recently been the subject of a threat lodged by two French airport operators to bring the State to ICSID, who refer to the Chile-French BIT's provisions on expropriatory conduct, fair and equitable treatment, and national treatment amidst the sharp drop in passenger volumes in the host country's largest international airport. The threat comes as the operators have failed to secure compensation for pandemic-induced losses and contract renegotiation in an attempt to preclude the risk of their investment from being expropriated. Allegations against Chile also include its reluctance to provide financial assistance and extension towards the concession that the two operators have requested to maintain the commercial feasibility of the investment. On the other hand, Chile's justification for such reluctance is two-fold. Firstly, financial assistance was refused on account of its share of losses within the revenue-sharing mechanism with the two operators. Secondly, Global Arbitration Review has also commented on Chile's refusal to provide compensation for pandemic-related losses and to renegotiate contracts owing to the legality and require further public tenders respectively.<sup>27</sup> Concerning the extension of the concession, Chile purportedly declined the request as the concessionaire is replaceable if they are unable to continue, which could be construed to mean that the Chilean government is willing to open another tender for the remainder of the operators' 20-year concession to 2035 should it decide to forego its investment.

Such a claim is representative of the possible Pandora's Box of investment treaty claims that could be opened should investors continue to feel that investment arbitration is the only way to salvage the amount they have invested into their failing investments which have fallen victim to the COVID-19 pandemic. From the perspective of host states faced with difficult decisions on safeguarding the trust of foreign investors and the health of their citizens, public finances must be taken into account as they continue to be allocated to the following. Not only do these finances bear the brunt in cases of mixed revenue-sharing schemes with private investors such as the case demonstrated above, but they also finance the deficits from the lessened inflows of cash owing to weak fiscal income, combined with the increased costs of sustaining the economy by alleviating the severe health and economic impacts of the COVID-19 crisis. Indeed, while Chile has not been the worst affected country in Latin America, its fiscal deficit for 2020 has been predicted to reach levels unseen since the 1970s,<sup>28</sup> an indicative sign that investment tribunals should consider when threats such as those above materialize into investment disputes.

#### **5. Possible Investors' claims filed against Indonesia**

Indonesia's actions to resolve the pandemic have been quite extensive, yet the success of its policies to deal with the growing number of infections has been limited. As of February 4th, 2021, the total number of COVID-19 cases accumulated to 4.4 million cases with a total of 144,000 deaths.<sup>29</sup> To contain the spread of the virus and its mutations, Indonesia enacted a variety of policies including but not limited to banning the entry of foreign nationals into its borders, limiting



labor mobility and access to the Indonesian economy for vital human capital to manage investment projects that often require skilled foreign workers to operate and conduct technology transfer to. In containing local transmission, regional and local governments have implemented large-scale social restrictions, permitting only certain sectors to operate, which involve limiting their operational hours and capacity level, thus reducing the revenue streams of enterprises heavily reliant on their offline operations. Areas heavily impacted by the government's measures include the retail, tourism, transportation, and financial sector. Furthermore, in an attempt to encourage businesses to continue fulfilling their contractual obligations, the government has introduced Presidential Regulation No. 12/2020. The regulation essentially stipulates that the COVID-19 pandemic cannot be used as grounds for invoking a force majeure claim, which poses concerns when the government decides to itself raise a force majeure defense in the event of an investment claim, thus heightening the urgency of the enactment of the proposed moratorium.

While these measures have largely aimed to control the spread of the virus and limit infection numbers, it needs to be asked whether these policies are effective when Indonesia remains the epicenter of ASEAN's largest COVID-19 outbreak. The apparent stance of the Government of Indonesia in its efforts to try and balance its health and economic objectives has not shown fruitful results as the economy has shrunk while an upward trend in the number of infected citizens continues to prevail. The rationale of these policies and their effect on investments of foreign nationals can be explored in greater depth should the prevailing risk of an investment claim give power to an arbitral tribunal to decide upon the appropriateness of these regulatory measures. It has been mentioned though, in the case of other countries with a similar situation to Indonesia, that investment tribunals are likely to grant substantial deference to states in exercising their regulatory powers to overcome the pandemic.

The electricity sector is one of the industries that may be prone to investment-related claims. The increased consumption of energy due to the pandemic has led the national electricity company (PLN) to take action to protect its cash flows. Action unfavorable to investors includes the limitation of power production by power plants and the request to the independent power producers to reduce production to the lowest end of the power purchase agreement.<sup>30</sup> As electricity consumption levels remain stagnant, PLN has also attempted to renegotiate its contractual provisions on its electricity purchases, with politicians exclaiming that they expect the renegotiations to result in a burden-sharing mechanism between the state power company and foreign investors.<sup>31</sup> While negotiations are ongoing, such a course of policies and decisions might reflect poorly on investors' perception of the electricity production regulatory climate in Indonesia, especially as such behavior by the state electricity company presents a recurring pattern to that of the high-profile arbitrations involving electricity purchase agreements with foreign investors.<sup>32</sup> Therefore, an escalation of events might result in threats of investment claims if their investments are subject to further prejudice. Another industry that has already faced the consequences of the pandemic is the construction industry, whereby revenue shortfall has resulted in numerous debt repayment suspensions and bankruptcy filings to foreign construction companies throughout Indonesia. There have been calls for the Indonesia Investment Coordinating Board (BKPM) to implement stricter verification measures for the entry of foreign construction companies,<sup>33</sup> signaling possible policy shifts towards a more restrictive investment climate for foreign investors in the construction industry and to a certain extent increasing the likelihood of claims from such investors.

Indonesia has been an ICSID member state since 1968, just one year after enacting its law on foreign investment. Ever since it has been subject to at least eight investment arbitration cases to date. These cases could proceed to arbitration owing to the relevant provisions in the respective IIAs as well as the national investment law which provides for international arbitration as a means of dispute settlement for foreign investors and the State. As evidenced in Article 32 (4) of Law No. 25/2007 on Investment, investment disputes between the Government of Indonesia and foreign investors shall be settled through international arbitration requiring the mutual consent of both parties. This provides the nexus for foreign investors to invoke the consent given by

Indonesia through the international investment agreements that it is a party to and thus resulting in an overly expansive net of disputes that could arise.

## 6. Right to regulate and the police powers doctrine

The right to regulate argues that host states are entitled to enact laws in pursuit of public policy objectives. The right to regulate was defined as “*the legal right exceptionally permitting the host State to regulate in derogation of international commitments it has undertaken through investment agreement without incurring a duty to compensate*.”<sup>34</sup> Subsequently, the right to regulate is a developing approach that emphasizes the sovereignty of the State to govern in pursuit of public interest with the examples of health, safety, and the environment. To benefit from the approach of the right to regulate, there has been a development of multilateral agreements that have adopted such provisions. One of the notable examples is prevalent in the Comprehensive Economic and Trade Agreement (CETA) between the European Union and Canada. On this notion, Article 8.9 on Investment and Regulatory Measures stipulates that the parties reaffirm their right to regulate within their territories to achieve legitimate policy objectives, such as the protection of public health, safety, the environment of public morals, social or consumer protection or the promotion and protection of cultural diversity. This provision implies that the right to regulate is explicitly acknowledged in the scope of certain public objectives. Article 8.9 of CETA further elaborates that the scope of the right to regulate includes the intervention of investors’ expectations.

Additionally, the OECD Negotiating Group on the Multilateral Agreement on Investment (MAI Negotiating Text) acknowledged the right to regulate. Related to this, the MAI Negotiating Text serves as the non-binding set of guidelines for the formulation of multilateral agreements. The affirmation of the right to regulate was stipulated in Article 3, which says that the contracting party may adopt, maintain or enforce any measure that it considers appropriate to ensure that investment activity is undertaken in a manner sensitive to health, safety, or environmental concerns, provided such measures are consistent with this agreement”. While the “right to regulate” is not explicitly articulated, the aforementioned formulation provides that public interest prevails as the reason for the State to regulate. Hence, the right to regulate may also be acknowledged implicitly by ensuring that investment activities should be conducted in line with public interests. After assessing the 24 BITs that are still in force, the pattern of the current BITs shows that investors are protected from non-compensated takings.

Public health is an area that has been included in past IIAs, with a recent example being the Australia-Indonesia CEPA, which provides for non-discriminatory regulatory actions by a Party that are designed and applied to achieve legitimate public welfare objectives, such as the protection of public health, safety, and the environment as not constituting expropriation. While Indonesia has not faced an investment claim brought against it on the grounds of public health, the provision in the Australia-Indonesia CEPA marks a milestone for both Australia and Indonesia, the former in consideration of the *Philip Morris Asia v. Australia* case brought against it in 2011 and as an example for the latter in forging regional trade agreements beyond its usual scope of partners (ASEAN plus framework).<sup>35</sup> This development presents itself as a useful reform in defining the scope of measures that are contemplated, highlighting that public health is one such area that deserves increased regulatory attention. Nevertheless, this promising case still does not mean that the right to regulate has been firmly established in Indonesian IIAs, and therefore an examination of the police powers doctrine is needed to see whether, in the case of Indonesia, it would present as a worthy defense against claims concerning the pandemic.

## 7. Can Indonesia rely on the doctrine of police powers?

Investment law acknowledges the doctrine of police powers, which emphasizes the State as the guardian of the general public interest.<sup>36</sup> A doctrine is a form of recognition of the State’s right to regulate foreign investment in their territories even if such regulation affects the investor’s property rights.<sup>37</sup> To provide a balance between State’s right to regulate and the investor’s property rights, the doctrine provides an exemption toward certain takings that would not

constitute an expropriation.<sup>38</sup> As part of customary international law, the application of the doctrine would not require compensation so long as the enacted State measure is non-discriminatory. A review of BITs in force shows that Indonesia is the party to disclose that the provisions on expropriation contain wording that allows expropriation for a “public interest”, “public order and morals”, “public benefit” and “especially important state needs”.<sup>39</sup> Provisions adopting the term “public interest” and “public benefit” require that such measures are adopted on a non-discriminatory basis, per the due process of law and against prompt, effective, and adequate compensation. However, by implementing the police power doctrine, states do not have a duty to compensate as such regulatory measures taken to protect public welfare would not amount to expropriation. To determine whether Indonesia can rely on the police powers doctrine, it is fundamental to understand the threshold of the doctrine in question. As one scholar correctly points out in her note by compiling the standards cited by a recent tribunal such as *Koch v. Bolivia* and *UAB v. Latvia*, the police powers defense would only prevail if the following are cumulatively fulfilled: the measure must be reasonable within the recognized police powers of the State, the measure is taken in conformity with due process, there is a public purpose, the measure is not discriminatory, the measure is proportionate, and the regulation must be bona fide.

The purpose of the government measure may exempt the conduct of expropriation in the enactment of police powers, especially if the purpose is to benefit the public. In the case of *Methanex v. the United States*, the dispute appeared when the State of California decided to establish measures that banned the use of additives that were polluting the water in the State. The tribunals rejected the claims brought by Methanex to protect the public.<sup>40</sup> In other words, it has been decided that the United States has exercised its police power for public purposes, rendering the action precluded from the duty of compensation. The author agrees with the majority approach of scholars reviewing health measures and international investment law, in that they do fall within the ambit of police powers. This is supported in the numerous case law that is present in the matter, among which *Philip Morris v. Uruguay* on the tobacco package labeling to reflect health concerns on cigarette consumption, *Chemtura v. Canada* on restrictions on the usage of agro-chemical lindane towards human inhalation of the substance and *Apotex v. the USA* on an import ban on generic drugs motivated by the State's concerns on the failure of product process controls. These various circumstances that tribunals have deemed as being within the realm of public health measures protected under the police power doctrine show that measures taken to tackle COVID-19 are also not an exception. A notable case concerning a taking by police authorities during the smallpox epidemic in 1903 also accepted the police power doctrine as a defense, despite the finding of a mistake by the authorities.<sup>41</sup> Such instances are also likely to happen during the current pandemic. In response to satisfying healthcare demands during the pandemic, states like Spain and Ireland have nationalized hospitals. With 70% of its hospitals owned privately, Indonesia had enacted a regulation that obliged 30–40% of hospitals' capacity for COVID-19 patients.<sup>42</sup> Eventually, this regulation disrupted private hospitals' cash flow, given the delay in receiving government funding for COVID-19 patients.

Additionally, the implementation of lockdowns, travel bans, and quarantine requirements for foreign visitors in Indonesia could also harm foreign investors with investments in the tourism and hospitality sector, as these measures cause a significant drop in the number of travelers. However, to the extent that these measures are enacted for a public purpose, Indonesia is precluded from the duty to compensate despite the correctness of such measures. To avoid states abusing this authority, it must be evident that the said public purpose was the legitimate reason for the disputed measure and not a disguise for the state's intention of frustrating foreign investment. An example can be taken from a current investor claim against Mexico. Concerning such a possibility, a scenario can be drawn to the warnings that the Mexican government has received from investors in the renewable energy sector regarding the anti-competitive legal reforms that regulators are trying to pass. The contentious point requiring analysis of the effects of the COVID-19 pandemic is when the Mexican government tries to defend its measures by raising the reduction of demand caused by COVID-19, whereas investors have alleged that COVID-19 was being used as an excuse by the state to allocate more market share towards its State-owned energy companies.<sup>43</sup>

## 8. Impact of the measure on investors

Tribunals usually assess the impact of the measure on the investor as an indicator to assess the compensation. This was coined as the “sole effects” approach as it does not consider the purpose of the regulation, but only the consequences imposed on the investment.<sup>44</sup> Specifically, investment tribunals will view the repercussions towards the economic value of the asset belonging to the investor, in which arbitral awards usually only allow compensation if there is a certain degree of damage. In *Pope & Talbot v. Canada*, the tribunals deemed that the damages were not “*substantial enough to be characterized as an expropriation*”. Hence, the measure did not create a significant impact on the degree of total value deprivation for the claimant. In other words, the claimant was still able to gain profit, meaning that the impact of the measure was not significant enough to prevent the claimant from using its assets such as in the *Sporrong and Lonnroth v. Sweden* case. The case did not amount to the conduct of indirect expropriation because the claimant was still capable of enjoying the right to enjoy the possession and continue to utilize their possessions. Therefore, an act of taking can be constituted as an expropriation if such interference creates substantial impacts which resulted in the deprivation of the fundamental rights of the foreign investors or the interference of the investment for a significant period.

## 9. Breach of legitimate expectation

In addition to all of the former, to distinguish between State’s legitimate regulation with regulatory expropriation, tribunals have raised the concern that such measures must not breach investors’ legitimate expectations.<sup>45</sup> For an expectation to be legitimate, there must be a specific commitment given by the government to the putative foreign investor that the government would refrain from imposing such regulation. Breaches of legitimate expectations can both contribute to a finding of expropriation and a violation of the fair and equitable treatment standard. The CCSI note continues to mention the challenges that states would face in their exercise of police powers, which include the extent to which it can be relied upon, the contradictory decisions by various investment tribunals, and the instance whereby a tribunal held that the police power doctrine is limited.<sup>46</sup> An argument that the note raised is the factual uncertainty over the developments over the novel pandemic, among which knowledge about the spread of the virus and the efficacy of the strategies governments have had in place based on their findings. This argument is then related to the daunting task that any member of a tribunal faced with a pandemic-related claim would have to consider, which is the reasonability of the measure concerning the deprived investor’s legitimate expectation. Such is the privilege that tribunals analyzing cases involving financial crises have, but those faced with a pandemic, unfortunately, do not.

Nevertheless, the world of investment arbitration has become a realm of international law where aspects of public law have been tested against the confluence of investors’ rights regarding investment protection obligations, along with newer variables such as human rights, environmental protection, and now, a spotlight on health epidemiology. As scientists continue to predict that COVID-19 marks the beginning of a new era of more viral diseases, the first award to reveal a tribunal’s analysis on the strength of a State’s defenses in the face of the pandemic would be highly reviewed and relied upon in further cases. As such, the reasoning of any tribunal faced with a pandemic-related case should factor into all the relevant facts that are present at the time that the decision was rendered, going insofar as to the government’s level of due diligence of COVID-19 related knowledge at the time of devising and enacting such regulatory measure and the true intent behind the implementation of such measures. In cases where the government does not base its decision on reasonable grounds or politically motivated decisions, instead of scientifically based ones while rendering foreign investors as sacrificial subjects to bear the impact of such a decision, the State’s defense might not bear some weight. This comes as the certainty of those factors outweighs the possible uncertainty surrounding the virus that states might raise in their resistance.

Concerning such a possibility, the Mexican government’s decision to terminate an investor’s license could be a cautionary tale of when governments breach an investor’s expectations of its long-term investment.<sup>47</sup> The tribunal in this case denied Mexico’s justification that such a measure

is due to the existence of public health concerns that arise from the investment. Instead, the tribunal found that the measure was based on community pressure that does not concern an emergency and is thus not reasonable with the deprivation of investors' expectations. Therefore, the key takeaway for States in enacting regulations to overcome public health concerns associated with the pandemic is to ensure that such measures constitute a reasonable response to an emergency. While social and political concerns can also arise from a State's public health policy,<sup>48</sup> the underlying reason to enact regulation must still be motivated by the public health issue itself to raise such justification as a defense.

#### 10. The focus of proportionality analysis in global health emergency

The final assessment is seen through the relationship between the purpose and impact of the measure, thus in determining the legitimate interest of investors against the goals of public policy, the indicator of proportionality is often considered.<sup>49</sup> The rationale behind analyzing the relationship between purpose and impact is to prove that the measure is an objective exercise of regulatory power and not a measure that is conducted to target a certain investor. Concerning deprivations and controls of property usage of investors by the State, then a proportionately reasonable and foreseeable national legal basis must exist as a form of stability, transparency, and the rule of law.<sup>50</sup> In *Tecmed v. Mexico*, the Tribunal weighed whether or not the measure of the government was "reasonable concerning their goals, the deprivation of economic rights and the legitimate expectations of who suffered such deprivation".<sup>51</sup> Here, the burden imposed on the investors and the purpose sought to be achieved through the measure must be proportionate. This proportionality will later be assessed by the court on a case-by-case basis, which also takes into consideration the expectations of the investors.

One of the examples of determining the proportionality of the measure is evident in the case of *Philip Morris v. Uruguay*, which concerns a tobacco investor that challenged a measure in pursuit of the public health interest of Uruguay. The tribunal adjudicated that the measure constitutes a "valid exercise of the State's police powers, with the consequence of defeating the claim for expropriation". Consequently, the applicant was incapable of attaining compensation for the losses occurring as a result of the measure. Commonly, most IIAs contain vague provisions related to the definition of public health, and thus the role of the tribunals is very important to determine whether a measure falls into the purpose of public health or not.<sup>52</sup> In this case, one of the considerations in the final decision by the tribunal was that Uruguay's tobacco control measures are reasonable and accountable because such measures have proven to be effective enough in reducing the consumption of tobacco. Hence, the correlation between the impact and the purpose of the measure allows the government to be justified in conducting an exercise of regulatory power. Certainly, while proportionality might not be an innovative analysis, one involving a public health emergency to the extent of the COVID-19 pandemic would be. This has led some scholars to argue that to justify the State's defense measures are necessary and proportional in a public health emergency, several factors should be considered, which include:

- a. issues that can only be resolved with an extensive policy consisting of an aggregation of interacting measures;
- b. the classification of a measure as either general government regulation or one directed at a particular investor, the former having a lower likelihood of being deemed expropriatory compared to the latter;
- c. the extent of proportionality and its variance over the period that the investor's investment has been affected, including that of the reasonableness of the measure at the beginning of the pandemic; and
- d. the fulfillment of the balancing exercise the government is tasked to restore public health objectives and their impact on foreign investors.<sup>53</sup>



Based on the analysis of the threshold of the police powers doctrine, while it can be posited that the doctrine is available for Indonesia to apply as a defense, a key consideration for the tribunal to take into account include the relevant facts present at the time the alleged act of injury was committed. In the case of Indonesia, several risks may pose a threat to the State, such as inconsistent travel policies and poorly coordinated structural organization in the management of the pandemic. On the former, experts have criticized that the policies are enacted based on inaccurate data and disregarding public health interests over economic motives, while the latter outlines that the structural inefficiencies of the agencies in charge of handling the pandemic translate to a weak response toward slowing the spread of the virus. One notable form of inconsistency was prevalent in the indecisive nature of regulating passenger transportation control in a cross-region traveling ban.<sup>54</sup> Hence, when faced with a case where the investor manages to highlight the unpredictable and unsuccessful measures that have caused injury to the investment, the police power defense might not prevail due to the very nature of the policy-making that both undermines the government's objective to contain the pandemic while depriving the investor's investment in the process.

#### **11. Can Indonesia rely on the security exception clause under Indonesia's BIT?**

In addition to the police power doctrine under customary international law, another method of defense that Indonesia may apply is the security exception clause. The presence of a security exception clause is rarely found in Indonesia BIT. Out of 26 BIT that are currently enforced, only 2 of them stipulate a security exception clause, with the example seen within the Indonesia-Qatar BIT. The wording of Article 7 of the BIT, states that *"This agreement shall not preclude [...] the fulfillment of its obligation concerning the maintenance or restoration of international peace and security, or the protection of its essential security interests"*. This stipulation translates to a wider scope of possible measures as it allows for not only the protection of domestic security interests but also international security. Security interests have been interpreted as states' protection of their territory and population from external threats. The determination of such a threat depends on the State's perception of the particular situation.<sup>55</sup> In addressing the challenges of the COVID-19 pandemic, States have taken preventive health measures that would restrict movement to reduce transmissions, such as lockdowns and travel restrictions. Take the example of Australia where the travel ban has effectively prevented the further spread of the virus by 85%.<sup>56</sup> These measures would not only enable a country to suppress the number of deaths in its territory, but also prevent other countries from recording imported infections. The number of fatalities that a state can avoid shows the necessity to implement such measures. To the extent that these measures are necessary to counter external threats arising from the pandemic, such as the number of deaths and the direct and indirect economic impact, these measures may be deemed as a state's security interest.<sup>57</sup>

The State's deference in determining its interest also has its limitations. Although the wording under certain security exception clauses appears as self-judging, such as the wording *"measure that [the state] considers necessary"*, State's measure will regardless be judicially reviewable. Consequently, any investment tribunal that has jurisdiction over the dispute may review whether the legitimate purpose of such a measure was to counter the pandemic or it was for some unlawful purpose. Therefore, despite the recognition of the State's sovereignty to regulate and enact laws for public health, any adjudicative body could ultimately review such measures after an alleged violation of international law, placing states in a vulnerable position as the repercussions of their policymaking could lead to an adverse finding by an investment tribunal. These varying degrees of interest standards could entail a different approach for Tribunals should claims arise that challenge Indonesia's measures. In any event, such a treaty provision signals one of the first lines of defense towards any purported claim of expropriation or violation of FET standards as it protects for States to exercise their regulatory powers to address such security concerns.



## 12. The need for a moratorium on the global stage

In light of the possible torrent of claims from investors as well as the limited defense available for states to avail, states may consider the enactment of a moratorium to prevent investment claims for a certain time. As discussed above, the presence of provisions in IIAs to preserve the right to regulate and to present the police power doctrine does not shield states from claims brought by investors willing to take the risk of those defenses. Investment claims are notoriously costly and time-consuming,<sup>58</sup> and although they provide an avenue for investors to claim their rights under investment protection instruments, claims that are brought during a global pandemic require the respondent state to allocate huge sums of money and human resources to defend against, when the funds can be allocated for public health purposes, specifically that of COVID-19 relief efforts. The proposed moratorium can overcome this concern as it does not rule out the possibility of claims by investors, but it allows a period whereby such claims are not faced and thus the opportunity on allocating its resources to the urgent agenda of maintaining its citizens' health and safety.

A moratorium, in its nature, is a temporary postponement or suspension. Therefore, it should be limited in duration.<sup>59</sup> The implementation of this moratorium should last throughout the COVID-19 pandemic, which is the state where the spread of the SARS-CoV-2 virus remains a pandemic, before its transitioning towards an endemic state. During the Ebola virus outbreak, the disease was no longer considered an international public health emergency when the spread of the disease had been controlled locally. However, using this threshold for the moratorium would be unfair to investors seeing that the severity of these two viruses remains incomparable. In contrast with the Ebola virus, the coronavirus is a pandemic, which conveys that the transmission of the virus has occurred on a global stage.<sup>60</sup> Moreover, the coronavirus is unlikely to subside in a near future given the continued mutation of the virus and thus creating further uncertainty for investors.<sup>61</sup>

In light of this, the moratorium should refer to the stage at which the pandemic evolves into an endemic state. Researchers have described the endemic state to mimic that of other respiratory diseases, which means that the virus remains likely to cause occasional outbreaks and epidemics. What differentiates the endemic state is the virus' spread pattern and coverage, which Callaway predicts can unfold in six different scenarios. The most probable of these scenarios is the continuous evolvement of the virus which would threaten the immunity that the current vaccines offer.<sup>62</sup> An adaptation must therefore be provided by constantly renewing the vaccine to combat the virus's newest mutation. Through this scenario, immunity will eventually increase and slow down the virus transmission. Although this would not stop the infection, however, the transmission would remain seasonal and concentrated in children or adults, depending on how the virus will evolve toward immunity. In any scenario, the transmission of the virus will no longer disrupt society and thus allowing for the moratorium to be revoked. The scope of the moratorium should include all investor claims to allow investors to invoke the dispute resolution clause in the relevant investment protection instrument. To enforce the moratorium, states may arrange such intent under a Memorandum of Understanding which is used by many countries as a common practice for countries to conduct multilateral or bilateral cooperation. In contrast to treaties, concluding an MoU does not require parliamentary involvement and thus can be easily enforced. Such a concise and swift procedure is useful for addressing urgent matters such as a moratorium during the pandemic. Although an MoU is a non-legally binding instrument, it is characterized by Article 31 (3) of VCLT as a subsequent agreement for interpreting a treaty. However, it is not the MoU that bears the legal weight but the State practice of implementing such political commitment under the MoU to interpret the treaty does.

Moreover, states may also create a joint interpretation to suspend investment treaty claims during the pandemic. Several states had also proposed this approach of creating a joint interpretation to create a consistent interpretation of provisions under investment treaties. Through joint interpretation, investors may reconsider their intention to claim before the investment tribunal according to its home-state agreement to suspend the effect of the treaty. If investors continue to pursue such recourse, the

proceeding may be ineffective for both parties as the investor's claim becomes weak when facing the joint interpretation as the State's defense. However, a multilateral instrument would require a longer time to be formulated and enforced as it would require many states to be involved in assembling the instrument. Therefore, creating a bilateral MoU could then become a reference for other states that have a similar intention. If a moratorium is arranged by bilateral and multilateral agreements, it ends by enacting a new agreement. If a moratorium is unilaterally declared and is a treaty-provided moratorium, it ends by enacting new unilateral acts, international agreements, or other forms of legal arrangements. If this ISDS proposed moratorium is either enacted within a specific period or even permanently, one could argue that it might get automatically terminated before the condition is stable therefore jeopardizing foreign investors' interest. This could also be an abuse of authority from the government.

To make it possible for the ISDS proposed moratorium to work and achieve its intended goal, it should not be arranged unilaterally. Therefore, the moratorium could not be terminated by new unilateral acts, but by a new agreement. Through this notion, it is proposed that the new agreement to end the moratorium should come from UNCTAD as the main United Nations body dealing with trade, investment, and development issues to officially declare that states can finally focus on investors' interests by the time the COVID-19 pandemic ends, in other words, there's no longer a need for an ISDS moratorium. Although the termination of the moratorium would be indefinite until further notice, governments should bear in mind that there needs to be a material change in international investment regulations, specifically in the current ISDS system. The duration where the moratorium is administered should be utilized to ease the situation, and provide a space for governments to focus on solving the crisis, without having to worry about upcoming claims from investors due to a breach of the FET standard, or expropriation under international law. As a country that has been vocal in the area of ISDS reform, Indonesia should also take on an active role in championing the moratorium. One such attempt is to submit working papers to raise the issue as part of the provisional agenda in the next session of the working group, as Indonesia has submitted similar documents in the past. Already, the support for the call for the moratorium on investment claims has been provided by non-governmental organizations from Indonesia and abroad, signaling public support for such a step.<sup>63</sup>

The effect of the moratorium should be in the form of a freezing effect under international law. To freeze the status quo implies that the current status is maintained and means that no changes to the current status of interest and claims are done. This effect requires an end to change at a point where either the moratorium is adopted or the moratorium regime specifies otherwise.<sup>64</sup> While the current reforms include detailed explanations on the establishment of a dedicated agency to facilitate investor-State channels of communication, increase information accessibility, and develop awareness among government officials, time-bound efforts are more focused on early detection/alert mechanisms to prevent escalation of investors' complaints into a dispute. They do not provide for a moratorium in exceptional circumstances such as the current pandemic, but rather maintain that effective management for accommodating investors' interests, and in any event that they are not accommodated and do escalate to a dispute, they are granted the right to bring claims upon an investment tribunal, so long as they fulfill the treaty provisions allowing them to do so. The current proposal champions a period whereby the ISDS regime is temporarily frozen concerning new submissions for disputes by investors until the resolution of the pandemic. Once the pandemic is over, new reforms should be enacted in the form of a permanent bar on all arbitration claims related to government measures enacted to address the economic, health, and social dimensions of the pandemic and its effects, in line with current trends in recently concluded bilateral investment treaties.

### **13. Protecting the interest of the state and the investors**

With its freezing effect, the moratorium provides the opportunity for states to ensure that the duration of the moratorium can be harnessed to develop more sustainable solutions, those that can balance the position and interest of both investors and the state through the ISDS mechanism.

Both state and investors' interests must be taken into account in implementing the moratorium. While states have the urgency to allocate funding towards the COVID-19 pandemic relief effort, investors might be concerned about their sudden inability to bring forward a claim before an investment tribunal. Although it is evident that ISDS proceedings leading to the rendering of an award take an average of more than three years to undergo, the possibility of a moratorium further extends this time frame for an investor contemplating the initiation of such proceedings by an uncertain duration. This extension could present itself as a liquidity issue for investors, who might, at a glance, suffer considerable losses from the postponement of a possible victory in securing a favorable award of damages from an investment tribunal. However, this is all under the assumption that the investor's only method of recovering their alleged losses is through an ISDS claim.

The proposal for a moratorium will not be implemented to entirely deprive such investors of recourse to other legal remedies, whether they be in the form of dispute prevention to counter the exacerbation of investor concerns into disputes, or through the provision of alternative dispute resolution mechanisms and/or local judicial and administrative remedies to ensure that the investor can be afforded a forum to bring forward their dispute. It is important to note that these processes should still have the objective of actually resolving the dispute, not as a mere forum to superficially provide a lackluster avenue that hosts claim while the moratorium is in place. Moreover, the moratorium could have a complementary effect on the mandated "cooling-off period" that is available in the relevant instrument containing an ISDS clause, adding more time for the parties to the dispute to explore other mechanisms available to settle. Ideally, these mechanisms can be effective in extinguishing the need for investors to resort to bringing their claims to investment tribunals altogether, by increasing the role of agencies that form the dispute prevention mechanism, the investment alternative dispute resolution framework, and subsequent judicial organs of the host states. States should take into account these mechanisms seriously to make the most utility of the moratorium period, as the "cooling-off" period has been read to only be in effect should there be an actual chance to resolve the dispute during such an interval.<sup>65</sup> Therefore, the complementary effect would only be realized if the State can demonstrate its legitimate efforts to resolve the dispute within the time granted under the moratorium.

#### **14. Promoting alternative dispute resolution**

The other means of dispute resolution that can be envisaged include ICSID Conciliation<sup>66</sup> and/or Mediation, which could provide an alternative forum for investors to address their concerns towards the government's actions that may adversely affect their investments, rather than taking an all-out approach on launching an investment arbitration claim, which would be subject to an investment tribunal's scrutiny in light of the great deference accorded towards state conduct during a health crisis. Recourse to domestic proceedings could be an option for investors who are protected under bilateral investment treaties that include exhaustion of the local remedies clause. Currently, the overwhelming majority of investment treaties are silent on the exhaustion of local remedies, neither explicitly requiring nor waiving the exhaustion of judicial or administrative remedies in the host country before invoking a claim before invoking an investment arbitration claim.<sup>67</sup> A recent example of this clause can be found in the 2007 Albania-Lithuania BIT, which says that if such a dispute cannot be settled amicably within six months from the date of the written notification provided in paragraph 1, and an [sic] domestic judicial and administrative remedies have been exhausted, the Contracting Party of the investor shall be entitled to submit the dispute either to [ICSID or ad hoc UNCITRAL arbitration].

Aside from the exhaustion of the local remedies clause, an alternative approach could take the form of pursuing local remedies for a specified amount of time before being able to submit their dispute to investment arbitration. For instance, the 1983 BLEU-Rwanda BIT explicitly mandates the exhaustion of administrative and judicial remedies, while simultaneously including that the requirement "cannot be invoked" after 18 months from the investor's written notification of the dispute. Additionally, several BITs provide that a dispute may only be submitted to arbitration if the specified period whereby a dispute continues to exist is elapsed. The practice has shown that

investment tribunals have consistently signified waivers from investment treaties that adopt a silent approach towards the exhaustion of local remedies, which has contrasted with the customary international law premise that applies is subject to an explicit waiver. Therefore, should a host state contemplate the utilization of such a clause, it should “expressly and unequivocally” indicate it, by providing that investors “shall” or “must” exhaust local remedies before instituting investment arbitration claims.<sup>68</sup> An illustrative example is the language used in the SADC Model BIT. Subsequent developments in investment protection could incorporate such provisions to solidify the claims brought by investors and familiarize domestic legal institutions with the type of disputes that foreign investors identify with, in the larger context of dispute prevention and policymaking. Moreover, as part of state reforms in the medium to long term, states may endeavor to develop their dispute prevention mechanism, a more “natural” mechanism that, if implemented correctly, could lead to not only a lessened amount of investor claims due to the accommodative nature of such a mechanism but also increasing the amount of foreign direct investment flows into the country as investors are attracted to the existence of institutions dedicated specifically towards addressing investor concerns. The availability of such a system would also contribute to the credibility of the State in terms of the State’s legal culture and the legal structure of foreign investment protection.

One notable example is that of the Peruvian dispute prevention mechanism, SICRECI, short for Coordination and Response System for International Investment Disputes, introduced in 2006. SICRECI’s main objectives include enhancing the public sector’s responsiveness and coordination in managing international investment disputes in a streamlined and pertinent approach. This is done by centralizing the collection of data on investment protection instruments the Peruvian State is a signatory to, establishing a warning system to alter developing international investment disputes, setting coordination flows and procedures for government entities involved in a dispute, and internalizing the costs arising from the involvement of such entities in a dispute. The system itself consists of the Coordinator, a Special Commission, and all of the government entities that have entered into agreements, according to rights or guarantees to national or foreign investors, or entities that represent the Peruvian State in agreements containing investment-related provisions. A central role is played by the Peruvian Ministry of Economy and Finance as the system’s Coordinator, which functions as a dispute identifier, tracker, and reviewer in receiving notices of disputes, and negotiation mechanisms while listing down Peru’s relevant investment protection instruments. The Special Commission acts as the mediator in the negotiations, managing human and financial resources for negotiations and case preparation, as well as allocating responsibilities that public entities bear in their involvement in the dispute.

Two main processes form the basis of SICRECI, which are communication and delivery of information regarding investment protection agreements and a notification system at the onset of a dispute. Additionally, SICRECI sets criteria to be fulfilled by public entities entering into investment agreements, to harmonize the approach taken by SICRECI members. These criteria include periods of direct negotiations, establishing alternatives to dispute resolution settlement systems, determining parties’ financial contributions arising out of their participation in the settlement or arbitration, and maintaining an obligation for investors to notify the System Coordinator for the beginning of the direct negotiation period. Since the enactment of Law No. 28,933 establishing SICRECI in 2006, there have been 23 ISDS cases initiated against Peru. Peru’s SICRECI system has, however, been praised for its effectiveness, particularly in addressing the number of cases brought against it, along with the broad nature of such cases.<sup>69</sup> This mechanism addresses the crux of the nature of the disputes that investors are often involved in, which frequently feature arbitrary government regulations followed by the lack of a forum for investors to consult the government in such changes that impact their investments. Indeed, out of the 11 cases against Peru that have been decided or settled upon since the establishment of the SICRECI system, six of those cases have been in favor of Peru, with two being in favor of the investor, two settings, and one case being discontinued. It is therefore worth highlighting that Peru’s approach might be one to follow for states wishing to take a more direct approach in addressing investor concerns at an

early stage, to localize the dispute, prevent further escalation to the extent of an investor-state claim, or in any event, increasing the State's chances of winning against a possible plaintiff. Moreover, States could also establish joint commissions or institutions to resolve investors' complaints. Such commission shall consist of the State representatives that could direct the issue to be reviewed and consulted with its counterpart in the host State to settle an emerging dispute. Therefore, several options can be enacted by States to protect both the interest of and investors. States should use the leeway given by the moratorium to dedicate their resources to the development of such a system as part of the package of reforms they might pass to restimulate the economy. Once the moratorium is lifted and states are susceptible to claims, they will have a mechanism allowing for these potential investor-state claims to be resolved internally.

### **15. Impact of the moratorium on the future trend of BITs**

Governments may also reshape their investment protection policies following the pandemic. The 2020 UNCTAD World Investment Report suggests that countries might be more conservative in screening foreign investment flows into their borders while also being more competitive in attracting foreign investment at the same time. Furthermore, the report states that countries are expected to amend their IIAs to incorporate relevant regulatory powers, and to take into account the public interest nature of their policies while simultaneously ensuring protection towards foreign investment. The UNCTAD initiative's goal is to launch the IIA Reform Accelerator in the summer of 2020. The program is designed as a policy instrument for countries that seek to accelerate the speed of reform of their existing IIAs to better suit the current investment climate and its associated challenges, along with sustaining safeguarding investments. While the report may be suggesting that reforms are being made, scholars have highlighted otherwise by remarking that the moratorium presents the opposite of progressing reforms, by viewing it as a roadblock instead,<sup>70</sup> as others rule out the proposal for a moratorium as being indiscreet.<sup>71</sup> The indiscreet nature of the proposal was lamented five main points- that the threat of ISDS does not result in a regulatory chill; that states have various agencies to manage the pandemic and ISDS claims; that investors are typically awarded smaller sums in the event of succeeding in their claim; the "creeping authoritarianism" phenomenon; and that the ISDS mechanism is part of the legal infrastructure designed to enforce the international rule of law.

As to the first point, the proposed moratorium is designed in mind the various regulatory actions that states have already taken, with the primary focus not being situated on alleviating the regulatory chill, but on shielding claims that arise from state measures enacted for and during the pandemic's course. These very state measures, enacted by the government that comprise different entities, prove the premise of the second point correct. However, the critic fails to understand that the cost of funding the defense to an investment claim deprives funding for other government entities, specifically those dedicated to the effort to relieve the pandemic's toll. Therefore, while it is also true that investors are awarded smaller sums if they win their claims, it is crucial to consider that states' budgets are already pressured to fund their legal battles against these investors. On that note, the concerns raised about the creeping authoritarianism and the international rule of law are noted and to that end, the proposed moratorium does not advance the notion that states should be left to regulate without honoring their obligations to investors, but rather it advances the idea that these claims can be brought after the moratorium is over and states can return to their proper condition and face these claims without worrying that they are sacrificing precious funds for public expenditure in fulfilling their country's needs on public health and other pandemic induced spending.

Admittedly, states have not responded to the initiative with the level of overwhelming support that would elevate its priority.<sup>72</sup> The reasoning for this might be the unprecedented nature of a moratorium as a policy approach that has not been contemplated by any government, along with the lack of academic discourse discussing it for it to reach the level of international discussions. While this article aims to advance the very proposal of the moratorium in discussing the arguments for it and the effectiveness that is brought by it in the context of the pandemic,

a heightened sense of urgency for states is needed at a decision-making level, to which the most appropriate forum to discuss would be UNCITRAL Working Group III on ISDS Reform. The Working Group's existing agenda items, while achieving considerable progress, do not feature time-sensitive and highly urgent matters such as that of the pandemic, and therefore the author agrees with a view expressed by a scholar at the UNCTAD conference to the extent that a more fundamental approach needs to be taken in addressing the social and economic impacts that the pandemic has had,<sup>73</sup> the response that governments have had towards it, and how ISDS factors into these considerations. To that end, the moratorium would help states to freely prioritize their citizens' public health and to maintain their economic activity without having to actively defend investor claims. The imposition of the moratorium might also harness mutually beneficial effects of dispute resolution, as the "cooling-off" period would allow investors and states to arrive at a settlement as to their points of contention, especially when supported by a strong dispute prevention mechanism such as the example outlined above. Should these benefits materialize as expected, this would dispel the fears of a torrent of claims that will continue to haunt states even after the pandemic has been resolved and the moratorium is lifted.<sup>74</sup> It is within every state's best interest that these sorts of provisions provide for just and comprehensive protection that they can enjoy in cases such as the COVID-19 pandemic. This is especially true when issues such as sustainable development which cover policy enacted on health grounds are being explicitly considered and thus present as an actionable defense for states that can rely on the more specific outline of the provision. Thus, these defenses limit any chance for an overly expansive interpretation of tribunals that has previously been the case in vague BIT provisions that do not directly tackle health issues or those that "borrow" norms of customary international law, which arguably serves as a more unpredictable path and outcome for states to follow through.<sup>75</sup>

## 16. Conclusion

The COVID-19 pandemic has caused and continues to cause the government to enact measures to protect public health. The prolonged pandemic has brought about numerous uncertain measures. Such measures may inflict adverse consequences on foreign investors including the disruption in the legitimate expectations of their investments. The aforementioned notion gives rise to the possibility of investors' COVID-19-related measure claims. Although there are customary defenses for states against the claim of COVID-19 such as force majeure, distress, and the police power doctrine, these defenses may not prevail due to high thresholds and strict interpretation by investment tribunals. As a result, governmental measures which are imposed for public health purposes may not preclude the payment of damages for investor claims. Thus, the current COVID-19 pandemic presents an increasingly difficult position for states to manage in balancing the interests of foreign investors and the well-being of their citizens. As a net recipient of foreign direct investment that has enacted numerous policies of its own to tackle the pandemic while contributing significantly to ISDS reforms, Indonesia's case is still one of high vulnerability to investment claims, which exemplifies the urgency not only for it but for other nations as well to push the for the multilateral agenda for the moratorium as a policy priority. Upon this balancing act, the proposed enactment of the moratorium on investment claims may allow states some respite concerning such claims during the pandemic. The proposed moratorium would allow their respective governments to realign their focus from defending against a wave of such claims towards more urgent matters in these unprecedented times while allowing these claims to be brought once the recalibration of health and economic conditions that allow for states to sufficiently allocate resources to defend against such claims has been achieved.

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## Notes

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