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# Beyond Diplomatic Protection: The Evolution of Investor Rights in International Law

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**Abstract**

The effectiveness and utility of diplomatic protection as a core mechanism for the traditional protection of investors' interests has been challenged with the rise of bilateral investment treaties (BITs) and investor-state dispute settlement (ISDS) mechanisms. While diplomatic protection remains advantageous in some cases, particularly in investment treaties without arbitration clauses, this essay analyses its limitations in terms of politicisation, high costs, inefficiency and lack of investor control. In contrast, the investment treaty arbitration mechanism offers a more rapid, independent and predictable means of dispute resolution. This essay concludes that diplomatic protection, while not completely obsolete, is no longer the most attractive instrument in modern international investment protection and is gradually being transformed into a complementary tool.

**Keywords:** diplomatic protection, international investment law, bilateral Investment treaties, Investor-State Dispute Settlement (ISDS), investment protection

## 1. Introduction

Traditionally, as the core means of protecting the rights and interests of investors between States, diplomatic protection has been valued for its place in international law. However, with the rise of new concepts such as Bilateral Investment Treaties, Investor-State Dispute Settlement and Fair and Equitable Treatment, the role and efficacy of diplomatic protection has triggered new discussions. This essay seeks to critically assess the attractiveness of diplomatic protection in modern international investment law by analysing its historical role, its modern application and its limitations, and by comparing it with the modern mechanism of investment protection, investment treaty arbitration, in order to argue that diplomatic protection is no longer the most attractive means for investors today.

## 2. Framework of Diplomatic Protection: Conceptual and Historical Evolution

Diplomatic protection is a customary international law institution that allows a State (the home State) to bring a claim on behalf of its nationality for an injustice suffered in another State (the host State).[1] Such protection is usually exercised when the national cannot obtain redress through any legal avenue in the host

[1] Viñuales, J. E. and Bentolila, D. (2012). 'The Use of Alternative (Non-Judicial) Means to Enforce Investment Awards against States'. In: Boisson de Chazournes, L., Kohen, M. G., and Viñuales, J. E. (eds.) *Diplomatic and Judicial Means of Dispute Settlement.* Leiden: Martinus Nijhoff Publishers, pp. 248-277.

State and must be based on a link of nationality between the individual and the State exercising the right of protection.[1]

In the mid-nineteenth century, with the rise of the imperialist era, this means of protecting their nationals and property in other countries by diplomatic means found favour with several States, particularly the established Western powers. As a result, diplomatic protection gradually became part of customary international law.[2] Diplomatic protection was regarded as a relatively new phenomenon of international law until 1913, when Borchard proposed that nationals should be protected by their home State while they were subject to the jurisdiction of the host State in a foreign country.[3] During this period, however, diplomatic protection was not limited to peaceful means. However, it was also subject to military intervention, which was criticised for its abuses by other Latin American countries. This led to the development of the Calvo doctrine, which was vehemently opposed to diplomatic protection.[4]

**3. Practice and Limitations of Diplomatic Protection**

Diplomatic protection has been criticised firstly for politicisation and inequality, as mentioned above, in opposition to the Calvo doctrine. Calvo states that home state intervention in the host state should be guided by the principle of reciprocity between states on an equal footing, "the recovery of debts and the pursuit of private claims does not justify *de plano* the armed intervention of governments", and developed European countries do not follow this idea of theirs when they exercise diplomatic protection against their investors in Latin America.[5] The practice of diplomatic protection has evolved and shifted from forceful intervention to peaceful means in modern times. However, it was still difficult to exclude the suspicion of power politics from resolving economic disputes, and many investee States continued to resist it. That resistance, in turn, limited the scope of diplomatic protection and made it more difficult for investors to obtain protection for their investments successfully through that means.

For investors, another distinct limitation of diplomatic protection in practice is its inefficiency and instability in resolving disputes.

Firstly, as mentioned earlier, diplomatic protection has two main requirements for preconditions that are onerous for the investor seeking protection. On the one hand, before seeking diplomatic protection, the investor is required to exhaust all local legal remedies in the host country.[6] This means that the investor must first attempt to resolve the dispute in the host State's judicial system, which can be time-consuming and costly. On the other hand, diplomatic protection requires a "link of nationality" between the investor and their home State.[7] This requirement may lead to complex nationality issues, especially where dual or corporate nationality is involved. For example, the International Court of Justice ruled in *Belgium v. Spain* that the nationality of a corporation should be determined by its place of incorporation. Accordingly, it rejected Belgium's attempt to exercise diplomatic protection on behalf of its nationals (the shareholders of Barcelona Traction, Light and Power Co., Ltd.) as the company's place of incorporation was Canada.[8] This means that, even though a company's shareholders may have the nationality of other States, the company can exercise diplomatic protection only by the State of its incorporation. Such a strict nationality requirement is undoubtedly a constraint for investors seeking more robust protection.

Secondly, for the investor, diplomatic protection remedies and results were not controllable. In international law, the remedies available for diplomatic protection are all based on State responsibility.[9] Thus, in the course of diplomatic

[1] Cuthbert, J. (1968). *Diplomatic Protection and Nationality: The Commonwealth of Nations.* Northumberland: Northumberland Press, pp. 4-7.

[2] Amerasinghe, C. F. (2008). *Diplomatic Protection.* Trans. Anonymous. Oxford; New York, N.Y: Oxford University Press, p. 14.

[3] Borchard, E. (1914). *The Diplomatic Protection of Citizens Abroad.* New York, pp. 497, 515.

[4] Tomz, M. (2007). *Reputation and International Cooperation: Sovereign Debt Across Three Centuries.* Princeton: Princeton University Press, pp. 114-157.

[5] Hershey, A. S. (1907). 'The Calvo and Drago Doctrines'. *The American Journal of International Law*, 1, pp. 26-45 at 27.

[6] Cuthbert, *Diplomatic Protection and Nationality,* p. 4.

[7] Ibid., p. 7.

[8] *Case Concerning Barcelona Traction, Light and Power Co., Ltd (Belgium v. Spain)* [1970] ICJ Rep. 3 (Second Phase), paras 70-71, 79.

[9] Polanco, R. (2019). *The Return of the Home State to Investor-State Disputes: Bringing Back Diplomatic Protection?* Trans. Anonymous. Cambridge: Cambridge University Press, p. 42.

protection, investors cannot participate directly in the settlement of disputes. Consequently, in diplomatic protection, the investor cannot participate directly in the dispute settlement and must rely on the diplomatic behaviour of the home State. This results in a lack of control by the investor in the dispute resolution process. Moreover, in theory, the injury that triggers diplomatic protection is then considered to have been suffered by the home state rather than the home state, and the claim is naturally based on state interests.[1] Compensation may then need to be obtained by the home State from the host State and then transferred to the investor.[2] However, the loss suffered by the investor may, in fact, be different from that suffered by the State, and there may be differences in the claims so that this indirect route to claiming compensation may result in an unfair or undesirable distribution of compensation to the investor.

**4. Challenges from Alternative Modern Mechanisms: Investor-State Arbitration**

In addition to the limitations of diplomatic protection itself, the rise of alternative dispute mechanisms, such as investment treaty arbitration, has led to a decline in its attractiveness.

Both bilateral and multilateral investment treaties typically give investors the right to initiate arbitration directly, enabling them to bypass the domestic court system of the host state and seek redress directly at the international level.[3] By resorting to investment treaty arbitration mechanisms, such as the ISDS, investors are allowed to initiate arbitration directly before international arbitral tribunals. They can assert their rights based on specific provisions in the investment treaty, including standards such as Fair and Equitable Treatment (FET) and Full Protection and Security (FPS).[4] In addition, the need to avoid tensions in diplomatic relations and possible political interference may also make some countries and investors more inclined to resolve disputes through arbitration.[5] Modern investment treaty arbitration mechanisms can be more attractive to investors than diplomatic protection, providing a relatively fast, independent, predictable and potentially less politicised means of dispute resolution.

**5. Conclusion**

In conclusion, diplomatic protection is becoming less attractive to investors in modern international investment law. Both because of its increasingly obvious limitations of politicisation, high cost and inefficiency, and uncontrollability, and because, as its modern alternative mechanism, investment treaty arbitration is more attuned to the value of international law's focus on the direct protection of the rights of the individual in the modern human rights era. That did not mean that diplomatic protection had become entirely obsolete. It still had unique advantages in certain specific situations, such as acting as a remedy when an investment treaty did not contain an arbitration clause or reconciling the positions of various parties in disputes involving several investors or States. However, it was clear that diplomatic protection was no longer the best and only way to seek protection for investment and that it would gradually come to fulfil its role as a complementary instrument.

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[1] Amerasinghe, *Diplomatic Protection,* p. 319.

[2] International Law Commission (ILC), *Draft Articles on Diplomatic Protection,* Art. 19.

[3] Lim, C. L., Ho, J., and Paparinskis, M. (2021). *International Investment Law and Arbitration: Commentary, Awards and Other Materials.* Trans. Anonymous. 2nd edn. Cambridge: Cambridge University Press, p. 295.

[4] Ibid., pp. 331-332.

[5] Kaufmann-Kohler, G. (2012). 'Non-Disputing State Submissions in Investment Arbitration'. In: Boisson de Chazournes, L., Kohen, M. G., and Viñuales, J. E. (eds.) *Diplomatic and Judicial Means of Dispute Settlement.* Leiden: Martinus Nijhoff Publishers, pp. 307-326, at p. 308.

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