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TEMPLARS ThoughtLab – **ISDS Series** | Part 1

Understanding Investor-State Dispute Settlement (ISDS)

Introduction

The protection of foreign investment has become one of the most significant and contested areas of international law in the twenty-first century. As cross-border investment flows continue to expand, the legal framework governing the relationship between foreign investors and host states has assumed a central importance in international economic governance.

The Investor-State Dispute Settlement (ISDS) system encompasses the framework of substantive protections, procedural mechanisms, and institutional arrangements enabling foreign investors to bring international arbitration claims against host states. Given Nigeria's position as a major recipient of foreign direct investment in Africa and its gradual emergence as a capital exporting country, understanding the ISDS system is of considerable importance for foreign investors operating in the country, Nigerian investors operating abroad, and the Nigerian state. In view of this, we have introduced the Templars ISDS Series to examine recent trends in the ISDS system. In this opening contribution, we introduce the ISDS system, its historical development and operational mechanics.

Historical Context

Early Development of International Investment Protection

The origins of international investment protection are often traced to the era of colonial expansion and the emergence of customary international law principles concerning the treatment of aliens and their property abroad. In the nineteenth and early twentieth centuries, capital-exporting states relied primarily on diplomatic protection and, in extreme cases, military force (colloquially referred to as 'gunboat diplomacy') to safeguard their nationals investing in foreign territories. This system was inherently political, dependent on the willingness of the investor's home state to espouse a claim on behalf of the investor, and fraught with the power asymmetries that characterised the international order of that era. As developing states gained independence in the 1950s and 1960s, they asserted their sovereign right to regulate and, where necessary, nationalise foreign-owned assets within their territories. Capital-exporting states responded by seeking predictable, depoliticised mechanisms to protect their nationals' investments abroad. In this context, the ISDS system emerged, with the bilateral investment treaty (BIT) as its principal instrument of international investment protection.

The Emergence of Bilateral Investment Treaties

The first BIT was concluded between Germany and Pakistan in 1959, establishing a precedent followed by hundreds of similar agreements in succeeding decades. Nigeria is signatory to a total of 31 BITs, with 14 currently in force.[1] These treaties typically provide foreign investors substantive protections including guarantees of fair and equitable treatment, protection against expropriation without compensation, and most-favoured-nation treatment alongside procedural mechanisms enabling investors to bring claims directly against host states through international arbitration.

The establishment of the International Centre for Settlement of Investment Disputes (ICSID) in 1965, pursuant to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention), marked a watershed in institutionalising the ISDS system. The ICSID Convention created a dedicated framework for arbitrating investment disputes between states and foreign nationals, providing procedural rules, a panel of arbitrators, and a self-contained enforcement mechanism that insulated awards from review by national courts.

Proliferation and Modern Development

The proliferation of BITs accelerated from the 1990s, driven by liberalised global capital markets and developing states' desire to attract foreign investment by committing to the rule of law and the protection of property rights. The global network of international investment agreements hit the 3,000 milestone in 2011 and by the end of 2025, the number stood at 3369.[2] This dense web of treaties has created a complex, sometimes overlapping, system of substantive protections and procedural options for foreign investors.

Investment Treaty Arbitration

Definition and Explanation

Investment Treaty Arbitration is a specialised form of international arbitration in which a foreign investor brings a claim against a host state, alleging a breach of substantive protections contained in an applicable investment treaty – which may either be a **Bilateral Investment Treaty (BIT)** or **Multilateral Investment Treaties,** in a national investment law or under customary international law.

The most frequently invoked standard of protection is the **Fair and Equitable Treatment (FET)** standard, which requires host states to treat foreign investors in accordance with principles of good faith, due process, non-discrimination, and proportionality. Another measure is the rule against **Expropriation**, and it encompasses both direct taking of property (nationalisation) and indirect expropriation, where regulatory measures substantially deprive an investor of the value or use of its investment without formal transfer of title. **Most-Favoured-Nation (MFN) Treatment** requires a host state to accord investors from a treaty partner, treatment no less favourable than that accorded to investors of any third state.

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[1] See https://investmentpolicy.unctad.org/international-investment-agreements/countries/153/nigeria

[2] This encompassed both bilateral treaties and multilateral instruments such as the Energy Charter Treaty and the investment chapters of regional trade agreements. https://investmentpolicy.unctad.org/news/hub/1794/20260421-international-investment-agreements-database-update-44-new-treaties-in-2025-and-evolving-drafting-practices

National Treatment obliges the host state to treat foreign investors no less favourably than domestic investors in like circumstances. **Umbrella Clauses** elevate contractual commitments made by the host state to the investor to the level of treaty obligations, enabling their enforcement through investment treaty arbitration.

Investment treaty arbitration derives its jurisdiction from the consent of the host state as expressed in the investment treaty. This consent – often described as a 'standing offer' or 'consent without privity' – permits an investor to initiate proceedings without a prior contractual relationship with the respondent state.

Purpose and Significance

The fundamental purpose of investment treaty arbitration is to provide foreign investors with a neutral forum for the resolution of disputes with host states, thereby reducing the political risks associated with cross-border investment. The system aims to promote the rule of law in international economic relations and to encourage flows of foreign direct investment by removing the resolution of investment disputes from domestic courts which may be perceived as lacking independence or impartiality in cases involving their own government.

The Investor-State Dispute Settlement System

Definition and Mechanism

The ISDS system is the procedural mechanism through which foreign investors, who are essentially private parties, are permitted to bring international law claims directly against sovereign states, before international arbitral tribunals, thereby departing from the traditional paradigm in which only states possessed legal capacity on the international plane.

The system operates through institutional channels such as ICSID, which administers arbitrations under the ICSID Convention and the ICSID Additional Facility Rules. Other frequently utilised frameworks include the UNCITRAL Arbitration Rules, the International Chamber of Commerce (ICC), the Permanent Court of Arbitration (PCA), among others.

Types of Disputes

The ISDS system addresses a broad range of disputes arising from the exercise of sovereign authority by host states. The most common categories include: claims arising from direct or indirect expropriation of foreign-owned assets; challenges to regulatory measures alleged to breach fair and equitable treatment standards; claims of discriminatory treatment of foreign investors relative to domestic investors or investors from third states; allegations of denial of justice by the host state's judicial system; allegations of breach of full protection and security; and disputes concerning the failure of host states to honour contractual commitments protected by umbrella clauses.

In recent years, the system has witnessed an expansion in the subject matter of disputes, with claims increasingly arising from energy transition, climate and other environmental regulation, public health measures, and the revocation of licenses and concessions. This expansion has intensified the tension between investment protection and the regulatory sovereignty of host states.

Nigeria and the ISDS system

There have been eight known ISDS cases against Nigeria. Four of those cases[3] were settled with the terms not made public. The fifth case, ***Interocean Oil Development Company & Anor v. Nigeria***[4] was heard on the merits and was subsequently decided in Nigeria's favour, marking Nigeria's first victory in investment treaty arbitration. Nigeria however suffered its first defeat in investment treaty arbitration in the case of ***Zhongshan Fucheng Industrial Investment Co. Ltd. v. Nigeria***[5] which was an ad-hoc investment treaty arbitration under the UNCITRAL Rules. In 2023, another ICSID claim was registered against Nigeria in ***Korea National Oil Corporation & Ors v. Nigeria***.[6] The proceedings are currently pending with the award being expected. The latest ISDS claim against Nigeria, ***Jupiter Lithium Ltd & Ors v. Nigeria***[7] was registered on 11 June 2026.

Challenges and Criticisms of the ISDS System

A. Consistency and Coherence

One of the most frequently cited challenges facing the ISDS system is the lack of consistency in arbitral awards. Because each tribunal is constituted ad hoc and there is no doctrine of binding precedent, different tribunals may reach divergent conclusions on substantially identical legal questions. The classic example is the pair of awards in *CME Czech Republic BV v Czech Republic* and *Lauder v Czech Republic*, in which two tribunals reached opposing conclusions regarding the same set of facts and the same governmental conduct.

B. Cost, Duration, and Accessibility

Investment treaty arbitration proceedings are notoriously expensive and lengthy. The costs of a typical case including legal fees, arbitrator remuneration, institutional charges, and expert fees routinely run into millions of United States dollars, whilst proceedings may extend over several years from commencement to final award. These characteristics present significant challenges for developing states, which may lack the financial and institutional resources to mount an effective defence, and for small and medium-sized investors, who may be effectively excluded from the system by its prohibitive costs.

C. Legitimacy and Regulatory Chill

Perhaps the most fundamental criticism levelled against the ISDS system concerns its implications for the regulatory sovereignty of host states. The phenomenon of 'regulatory chill' describes the tendency of states to refrain from adopting legitimate public interest regulation in areas such as environmental protection, public health, and labour standards for fear of triggering investment treaty claims and substantial financial liability. This concern is of particular relevance to developing states, including Nigeria, where the need for robust regulatory frameworks in areas such as the extractive industries must be balanced against the obligations assumed under investment treaties. Additional criticisms include allegations of pro-investor bias in the system, the perceived lack of transparency in proceedings, and

[3] *Guadalupe Gas Products Corporation v. Nigeria* (ICSID Case No. ARB/78/1); *Shell Nigeria Ultra Deep Limited v. Federal Republic of Nigeria* (ICSID Case No. ARB/07/18); *Eni International B.V. & Ors v. Federal Republic of Nigeria (ICSID Case No. ARB/20/41); and Shell Petroleum N.V. & Anor v. Federal Republic of Nigeria* (ICSID Case No. ARB/21/7).
[4] *Interocean Oil Development Company & Anor v. Federal Republic of Nigeria (ICSID Case No. ARB/13/20)*.
[5] https://www.italaw.com/cases/9287 Final Award 26 March 2021.
[6] *Korea National Oil Corporation & Ors. v Federal Republic of Nigeria (ICSID Case No. ARB/23/19)*.
[7] *Jupiter Lithium Ltd & Ors v. Federal Republic of Nigeria (ICSID Case No. ARB/26/27)*.

broader concerns regarding the legitimacy of a system that permits unelected arbitrators to pass judgement on the exercise of sovereign regulatory authority.

D. Reform Efforts

In response to these challenges, significant reform efforts have been undertaken, the most prominent of which is the work of UNCITRAL Working Group III on Investor-State Dispute Settlement Reform, which has been engaged since 2017 in a comprehensive review of the system with a view to identifying concerns, developing reform options, and building consensus on a reformed framework. One of the suggestions on the table is the establishment of a Multilateral Investment Court (MIC), featuring permanently appointed judges, an appellate mechanism, and enhanced guarantees of independence and impartiality.

At the regional level, African states have developed approaches tailored to their specific concerns. The African Union's Pan-African Investment Code (PAIC) seeks to balance investor protection with sustainable development objectives, embedding investor obligations and emphasising the right of host states to regulate in the public interest. These initiatives are of direct relevance to Nigeria's approach to investment treaty-making and its engagement with the broader ISDS reform discourse.

Conclusion

The ISDS system remains a remarkable innovation in international law, granting private parties direct access to international adjudicatory mechanisms for the resolution of disputes with sovereign states. From its origins in the post-colonial era, the system has grown into a vast and complex regime, underpinned by thousands of investment treaties and administered by multiple institutional frameworks. Yet the system faces profound challenges. Concerns regarding consistency, cost, legitimacy, and the implications of investment protection for regulatory sovereignty have generated a robust reform discourse.

For clients and Nigerian legal practitioners who engage with the ISDS system, a thorough understanding of both its operational mechanics and the broader normative debates surrounding its legitimacy and reform is critical. As Nigeria continues to attract significant foreign investment coupled with the increased investments by Nigerian investors abroad, the importance of this understanding will only grow.

The future of the ISDS system will be shaped by the outcome of ongoing reform processes and by the choices made by states regarding the design of their investment treaties and the institutions to which they entrust the resolution of investment disputes. Subsequent instalments of the Templars ISDS Series will address in fuller detail the different protection measures available under the ISDS system and the defences available to host states to safeguard their interests. It is hoped that this first instalment has provided a useful foundation for engagement with these critical questions.

If you require any further information, do not hesitate to contact us.