AVOIDING LIABILITY FOR HUMAN RIGHTS VIOLATIONS IN PROJECT FINANCE

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I. INTRODUCTION

It’s dangerous out there, especially when companies venture into the developing world. The risks come to mind easily: currency, expropriation, regulatory, political violence, legal, and performance. One risk has attracted little attention in the project finance community despite its sensational nature and its difficulty to mitigate: lawsuits in the United States against project sponsors for human rights violations allegedly committed outside the United States. Although this “human rights risk” has seldom come up, energy companies such as Texaco, Unocal, Shell, Chevron, and Exxon Mobil have discovered, this risk exists in the realm of project finance.

This paper first analyzes the legal theory behind the human rights risk and Unocal, the lead case to have developed the doctrine. The paper then

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3. “Liability for human rights violations risk” is more accurate, but too unwieldy a name for this risk; accordingly, the paper employs “human rights risk.”

examines in detail the human rights risk and suggests means of identifying and mitigating it.

II. THE ALIEN TORT CLAIMS ACT

The Alien Tort Claims Act\(^5\) (ATCA\(^6\)) is relevant to the project finance community because it dispenses with traditional notions of jurisdiction in allowing foreign plaintiffs to sue in United States courts for torts committed abroad. Congress passed the ATCA as a part of the Judiciary Act of 1789.\(^7\) The ATCA provides that “[t]he district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States.”

A. History

Although scant legislative history exists, scholars believe that Congress passed the ATCA to afford redress before American courts to foreign ambassadors and ships attacked by pirates.\(^8\) Of the twenty-odd cases brought under the ATCA between 1790 and 1980, in only two did the court determine that it had jurisdiction to hear the case and that the plaintiffs had a cause of action.\(^9\) In 1980, however, the U.S. Court of Appeals for the Second Circuit resurrected the ATCA into a potent weapon for the human rights community when it held in Filartiga v. Pena-Irala that federal courts could hear claims for violations of international law suffered by aliens outside the United States against defendants located within the United States.\(^10\) Since Filartiga, numerous courts have followed the Second Circuit in recognizing the jurisdiction of federal courts over claims brought under the ATCA.\(^11\) Although no ATCA cases have reached the Supreme Court, it is now well settled that aliens may sue in the United States for violations of international law suffered abroad.\(^12\)

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6. Controversy surrounds even the abbreviation of this statute. According to John Reynolds, partisans of using 28 U.S.C. § 1350 against corporations attempt to elevate its status by referring to it as an “act,” i.e., the “ATCA;” while persons in the other camp refer to it as a “statute,” i.e., the “ATS.” Interview with John C. Reynolds, attorney with Jones, Walker, Wachtler, Pontevedt, Carrere & Denegre, L.L.P., in Austin, Tex. (Apr. 14, 2000). This paper employs the abbreviation ATCA, not out of partisanship, but because it is the most commonly used abbreviation today.
7. Judiciary Act, 1 Cong. Ch. 20; 1 Stat. 73 (1789).
10. Stephens & Ratner, supra note 9, at 8 and n. 6.
11. Filartiga v. Pena-Irala, 630 F.2d 876, 878, 885-87 (2d Cir. 1980) (holding that torture occurring in Paraguay violated the law of nations). Id. at 884.
B. Elements of the ATCA

The elements of the ATCA require: (1) an alien to (2) allege a tort that (3) violates the law of nations.\textsuperscript{14} The first two elements are straightforward and rarely present controversy. ATCA litigation often hinges on the third element: violation of the law of nations.

1. Covered Harms

Courts have been attempting to determine what qualifies as a violation of the law of nations for years. Courts agree generally on the standard - that which is universally condemned as of the time of the litigation - but have demonstrated less unanimity in its application.\textsuperscript{15} Nonetheless, decades of litigation under the ACTA have led courts to recognize the following crimes as violations of the law of nations under the ACTA: torture, extrajudicial executions and disappearances, arbitrary detention, genocide, war crimes, slavery, slave trading, and crimes against humanity.\textsuperscript{16} Cruel, inhuman and degrading treatment, and a systematic pattern of violations have been deemed gross human rights violations, but have yet to be adjudicated under the ATCA.\textsuperscript{17} Finally, the federal common law has not recognized environmental harms, cultural genocide or ethnocide, and the cultural destruction of peoples as binding international law. Some commentators say that the law may one day accommodate these harms, however.\textsuperscript{18}

2. State Action

Although the ATCA is silent with respect to state action, courts have held that certain crimes, such as torture and summary execution, constitute violations of international law only when committed by state officials or under color of law. Other crimes such as slavery, slave trading, piracy, and certain war crimes, constitute violation of international law whether committed by state officials or by private individuals not under color of law.\textsuperscript{19}

C. Related Laws

1. Act of State Doctrine

Defendants in ATCA actions often invoke the act of state doctrine. The act of state doctrine provides that U.S. courts should not question the validity of sovereign acts of foreign states, lest the judiciary interfere with

\textsuperscript{14} 28 U.S.C. § 1350.
\textsuperscript{15} Filartiga, 630 F.2d 876, 888 (2d Cir. 1980).
\textsuperscript{17} Id. at § 17.
\textsuperscript{18} Tzeutschler, supra note 12, at 364, 405-18.
\textsuperscript{19} Kadic v. Karadzic, 70 F.3d 232, 239-42 (2d Cir. 1995), reh'g'g 74 F.3d 377, on remand, cert. denied 518 U.S. 1005 (1996).
the conduct of American foreign policy by the executive and legislative branches and imperil amicable relations with other nations.\textsuperscript{20} Courts generally disregard the act of state doctrine if the executive branch has indicated that it does not object to a court's examination of the validity of acts of a foreign state\textsuperscript{21} or if the issue presented is unlikely to affect foreign relations.\textsuperscript{22}

Since the act of state doctrine applies only to valid acts of a state,\textsuperscript{23} corporations face particular difficulty in invoking this doctrine as a defense. Even if a corporation qualifies as a state actor, its acts are not entitled to the same level of deference as those of a state.\textsuperscript{24} Furthermore, because ATCA suits against corporate defendants will probably not sour relations between the United States and other nations, courts are unlikely to recognize the act of state doctrine as a ground for dismissing an ATCA claim against a corporate defendant.\textsuperscript{25}

\section*{2. Foreign Sovereign Immunities Act}

A primary limitation on the ATCA is the Foreign Sovereign Immunities Act (FSIA), which grants foreign governments broad immunity from suit in the United States.\textsuperscript{26} Unlike the act of state doctrine, which is a doctrine designed to avoid overreaching by the judiciary, the FSIA stems from the international law concept of sovereign immunity.

In \textit{Argentina Republic v. Amerada Hess Shipping Corp.}, the Supreme Court ruled that the FSIA prevented the bringing of a suit against a foreign sovereign pursuant to the ATCA.\textsuperscript{27} The FSIA may protect governmental corporations from ATCA claims, but such protection would not extend to private corporations engaged in business ventures with governmental corporations.\textsuperscript{28}

\textsuperscript{23} Flatow \textit{v.} Islamic Republic of Iran, 999 F.Supp. 1, 24 (D.D.C. 1998). The act of state doctrine presumes that official acts of a state are valid. Sampson \textit{v.} Federal Republic of Germany, 975 F.Supp. 1108, 1121 (N.D. Ill. 1997). Although an act need not be legal under U.S. or international law for it to be valid, certain acts so exceed the bounds of acceptable conduct that they are not valid under the act of state doctrine. \textit{Flatow}, 999 F.Supp. 1 at 24 (stating that assisting an intrafamilial kidnapping by providing a travel visa is a valid act of state).
\textsuperscript{24} Banco Nacional de Cuba \textit{v.} Sabbatino, 376 U.S. 398 (1964).
\textsuperscript{25} Tseuzechler, \textit{supra} note 12, at 371.
\textsuperscript{26} 28 U.S.C. §§ 1330, 1332(a), 1391(f) and 1601-1611 (2001).
D. Procedural Aspects of the ATCA

1. Jurisdiction

Defendants in ATCA cases have a variety of procedural defenses at their disposal. First, and most obvious, is lack of personal jurisdiction. Naturally, this strategy is rarely an option for American companies, which cannot avoid jurisdiction in the United States.

2. Forum Non Conveniens

Defendants in ATCA cases raise the forum non conveniens doctrine routinely because the torts underlying ATCA claims necessarily take place outside of the United States. Courts grant forum non conveniens motions only if an adequate forum exists elsewhere, however. Texaco, for instance, when faced with an ATCA claim in a United States court for environmental torts committed in Ecuador, invoked forum non conveniens in an attempt to have the case moved to Ecuador. The court granted Texaco's motion, on the condition that "Ecuador provide an adequate alternative forum." Following a coup d'etat in Ecuador, the court reiterated its stance that dismissal for forum non conveniens requires the availability of an adequate alternative forum and ordered the parties to make submissions regarding the likelihood that the courts of Ecuador or Peru "might reasonably be expected to exercise a modicum of independence and impartiality . . ."32

3. Failure to Join an Indispensable Party

Defendants may try to join a foreign state as an indispensable party and then argue that the FSIA precludes United States courts from hearing a suit against the foreign state in question. If successful with these two arguments, the defendant may then ask the court to dismiss the suit for failure to join an indispensable party. Courts will often issue rulings that allow the plaintiff to obtain the desired remedy without the involvement of the foreign state, thereby obviating the force of a dismissal for failure to join an indispensable party.33

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32. Id. at *10. It is probably for this reason that plaintiffs' complaint in the Exxon ATCA suit states that plaintiffs do not have access to an adequate legal system in Indonesia, the site of the alleged torts, and that bringing suit in Indonesia would invite retribution and punishment. Complaint, Doe v. Exxon Mobil Corp., ¶ 3, (D.C. Cir. June 11, 2001), available at http://www.laborrights.org (last visited July 8, 2001).
33. Tzetschler, supra note 12, at 363-64, 387-405; Stephens & Ratner, supra note 9, at 63-95.
III. THE UNOCAL LITIGATION

A. Introduction

If Unocal Corporation, a California oil company, wins an appeal before the U.S. Court of Appeals for the Ninth Circuit, the company will finally put an end to six years of legal battles in federal court against plaintiffs from Burma.34

The allegations against Unocal have made their way into countless newspapers and other media over the past six years, including the front page of the Los Angeles Times. An editorial in the New York Times, an article in Newsweek, and reports on Nightline and NPR's All Things Considered have all reported the allegations.35 In addition, Unocal will have spent considerable money and energy battling plaintiffs from Burma. Consumer boycotts and other forms of public opposition will have hurt Unocal's profits.36 Shareholders have begun to question Unocal's activity in Burma.37 Furthermore, a federal district court ruled recently that the

34. As of July 20, 2001, the two cases concerning Unocal's activities in Burma, National Coalition Gov't of Union of Burma v. Unocal, Inc., 176 F.R.D. 329 (C.D. Cal. 1997) and Doc v. Unocal Corp., 963 F. Supp. 880 (C.D. Cal. 1997) had 361 and 620 entries respectively (CourtLink search conducted on July 20, 2001). Whether to identify the country as Burma or Myanmar is itself a contentious topic. This paper follows the terminology of the court that examined this case most recently: "Burma" refers to the country and "Myanmar" refers to the government ruling the country. See generally Doc v. Unocal Corp., 110 F. Supp. 2d 1294 (C.D. Cal. 2000)[hereinafter Unocal II].


37. On the Nightline program, Harvard Business School Professor Deborah Starr said that the public opposition was doing “real damage to Unocal’s moral and business brands.” She pointed out that despite the considerable stock market increases recently, Unocal's stock prices have remained flat throughout. Nightline, supra note 35. On the other hand, Unocal reported its highest ever quarterly earnings on April 25, 2001, though this increase can be attributed in large part to a strong rise in the price of natural gas in the United States. Unocal Posts Record Quarterly Earnings, PR NEWSWIRE, Apr. 25, 2001.

38. During Unocal’s latest shareholders’ annual meeting, two resolutions related to Unocal’s investment in Burma came to a vote: the first, calling on the Unocal board of directors to adopt, implement, and enforce a code of conduct based on the United Nations' International Labor Organization conventions on workplace human rights, received support of 23.3%, and the second, urging the appointment of a special committee of the board to review ways to link executive pay to the company’s ethical and social performance, obtained support of 15.6%. Despite their failure, these two resolutions ranked, among 138 social policy shareholder resolutions that came to a vote in the spring and summer 2001 annual meeting season, first and fourth, respectively. See also AFL-CIO and ICEM Protest Uno-
plaintiffs' claims under state law in California may proceed in state court.39 If the plaintiffs can convince the Ninth Circuit to overturn the district court's grant of Unocal's motion for summary judgment, then farmers and fishermen from southern Burma will testify in detail about how they were relocated against their will, subjected to forced labor, assault, rape, torture, and saw friends and family murdered by the Myanmar State. The case could also establish legal precedent that would affect energy projects throughout the world, as other plaintiffs would litigate in the United States against corporations for human rights abuses committed on foreign soil by a corporation's business partner.

B. History of the Yadana Project

The Yadana ("treasure" in Burmese) field, in the Andaman Sea off of the southern coast of Burma, has been estimated to contain 9.6 trillion cubic feet of natural gas reserves.40 In September 1994, a consortium comprising Unocal, Total S.A. of France, the publicly owned Myanmar Oil and Gas Enterprise (MOGE), and the Petroleum Authority of Thailand (PTT), agreed with the Myanmar government to build a 260-mile pipeline41 from the Yadana offshore field to the Ratchaburi region of Thailand. Total's stake in the project is 31.24%, Unocal's is 28.26%, PTT's is 25.5%, and MOGE's is 15%.42 The $1.2 billion pipeline marked Burma's biggest ever business venture with foreign partners.43 The same month, Unocal and Total entered into a take-or-pay sales agreement with the PTT whereby the agreement stated the PTT would take 65 million cubic feet per day as of August, 1998, to fire a 2,800-megawatt power plant in the Ratchaburi region of Thailand.44 The excess was to go to Burma45 for a fertilizer plant and a power facility.46 The sponsors anticipated that produc-

39. On March 5, 2001, the Federal Court for the Central District of California issued an oral ruling stating that plaintiffs' state-based claims could be heard in state court during the appeal to the Ninth Circuit. Telephone interview with Natacha Thys, Assistant General Counsel, International Labor Rights Fund, who argued the motion (July 20, 2001).
40. Ron Corbin, Unocal Increases Burma Field Natural Gas Reserves by 60 Percent, J. OF COM., Nov. 5, 1996, at 7B.
42. Millman, supra note 2, at 17.
45. Buchan & Barnes, supra note 43; Yadana Gas Contract Change Proposed, supra note 44.
tion of natural gas would ultimately reach 650 million cubic feet per day, but the project has yet to hit full capacity, as facilities in Thailand remain unfinished. The project was expected to be financed exclusively with equity and would include some Export Credit Agency (ECA) support, but not from ECAs in France, the United Kingdom, or the United States. Lehman Bros. analysts Paul Cheng estimated that the project could increase Unocal's per share earnings up to 10% annually. Total took the lead in developing the field and in constructing and operating the pipeline to the Thai border and the PTT built the stretch of pipeline from the power plant to the Thai border. Total manages the project.

The sponsors also sought to improve the lives of the inhabitants around the project site. The consortium built or renovated eight schools, established a shrimp farm and more than 100 pig, cattle, goat, and poultry farms. The sponsors installed electricity in four villages and hired twelve full-time doctors. Hervé Madéo, the president of the consortium, explained that through these deeds the sponsors attempted to establish a sense of community among the project and the surrounding inhabitants. "If we want to integrate this project into the community, this must be their pipeline," Madéo added. Furthermore, the consortium agreed to pay one million dollars to compensate villagers for 525 acres of land and it has adopted a policy of paying the local inhabitants that work on the project.

Nonetheless, the pipeline, which traverses a sensitive area that has been the site of much fighting between the government and rebel groups, faced opposition. This became obvious in March 1996, soon after construction of the pipeline began, when an armed group ambushed a pipeline convoy, killing five Total employees and wounding another eleven. The consortium allegedly entered into a security pact with the Myanmar military, which consists of young, underpaid, and untrained troops, to provide protection for the project.

49. ECAs are governmental or quasi-governmental entities that subsidize and promote a country's exports and investment abroad. Prominent ECAs include the Export-Import Bank and the Overseas Private Investment Corporation (U.S.), COFACE (France), Hermes (Germany), and the Japan Bank for International Cooperation and the Nippon Export and Investment Insurance (Japan).
50. Millman, supra note 2, at 17.
51. Id.
52. Buchan & Barnes, supra note 43.
54. Iritani, supra note 46.
55. Id.
56. Branigin, supra note 43.
57. Id.
58. Iritani, supra note 46.
C. The Unocal Cases

1. Plaintiff’s Claims

Conflict did occur, and in 1996, Burmese affected by the Yadana project brought suit in the United States District Court for the Central District of California in two separate actions: John Does against SLORC, MOGE, Total, Unocal and some of its officers, and John Does against Unocal. The plaintiffs claimed that the defendants had relocated villagers against their will, subjected them to forced labor, stolen the villagers’ property, and committed other human rights abuses, including murder, assault, rape, and torture. Specifically, the plaintiffs alleged violations of the Alien Tort Claims Act, the Racketeer Influenced Corrupt Organizations Act, the Torture Victims Prevention Act, several international laws, unfair business practices, and various tort actions pursuant to California law. The plaintiffs sought injunctive relief and damages in excess of one billion dollars.

2. Procedural Rulings

Unocal argued that SLORC was an indispensable party, and because it could not be joined as a result of its sovereign immunity, the suit should be dismissed. The court responded that SLORC was not an indispensable party because the plaintiffs could obtain the monetary and injunctive relief they sought without SLORC. Therefore, the suit could proceed with Unocal as the sole defendant.

Unocal also invoked the act of state doctrine in arguing that the court had no authority to review acts of SLORC and MOGE. The court responded, however, that since “nations do not, and cannot under international law, claim a right to torture or enslave their own citizens, a finding that a nation has committed such acts . . . should have no detrimental effect on the policies underlying the act of state doctrine.” Because the executive branches had condemned SLORC for its human rights abuses, the court concluded that “it is hard to imagine how judicial consideration of the matter will so substantially exacerbate relations as to cause ‘hostile confrontation.’” As a result, the court held that the act of state doctrine

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61. Judge Richard Paez presided over all litigation relating to the Yadana field project until his confirmation for the Ninth Circuit Court of Appeals in March, 2000. Judge Paez’s pro-plaintiff rulings in the Unocal cases caused some controversy during the confirmation hearings. See also Jason Hoppin, Chevron’s Nigerian Quagmire, THE RECORDER, Apr. 10, 2000. Judge Ronald S.W. Lew took over after Judge Paez.
63. Id. at 26.
65. Id. at 894.
did not prevent the court from reviewing SLORC’s acts. In a related suit, however, the same court held that the act of state doctrine precluded review of claims by certain John Doe plaintiffs for alleged expropriation by SLORC of property located in Myanmar. The court reasoned that, since governments take property within their own territory for a variety of reasons, the determination of the validity of expropriation is best left to the executive branch.67

As a result of other procedural motions, Total was dismissed for lack of personal jurisdiction68 and class certification for all similarly situated persons from the area affected by the Yadana pipeline was denied.69 The plaintiffs withstood Unocal’s motions to dismiss for lack of subject matter jurisdiction and failure to state a claim.70 The court consolidated the two Unocal suits and in August, 2000, granted Unocal’s motion for summary judgment for the reasons explained below.71 The plaintiffs have appealed to the U.S. Court of Appeals for the Ninth Circuit, which will hear oral argument in late 2001 or early 2002.72

3. The Substantive Rulings

a. State Actor Under the ATCA

The U.S. District Court for the Central District of California considered the state actor requirement for ATCA claims upon Unocal’s motions to dismiss for failure to state a claim (Unocal I)73 and Unocal’s motion for summary judgment (Unocal II).74 Because plaintiffs alleged torts by Unocal in both categories, including torture, rape, and other forms of physical violence in the former category and forced labor in the latter category, the Unocal I and Unocal II courts examined Unocal’s alleged violations of international law as both a state actor and a private individual. The two courts analyzed Unocal’s status as a state actor through the lens of title 42 of the U.S.C., section 1983,75 which is the standard used for this purpose in ATCA litigation. The Unocal I case, presided over by Judge Paez, and the Unocal II case, presided over by Judge Lew, reached strikingly differ-

72. Thys, supra note 39.
75. 42 U.S.C. § 1983 (1984), “Civil action for deprivation of rights,” states “[c]very person who, under color of any statute... of any State... subjects... any person... to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law...”. Id.
ent standards for defining a state actor under the ATCA. Presumably, this discrepancy between the definition of state actor will be a principal issue before the Ninth Circuit.\footnote{Thys, supra note 39.}

b. \textit{Unocal I - Knowledge Suffices}

Most significant, in the \textit{Unocal I} decision, from the point of view of project sponsors, is the holding that mere knowledge of a project participant’s violation of the law of nations and acceptance of benefits flowing from such violations suffices to impose liability on a private company for human rights violations.\footnote{\textit{Unocal I}, 963 F. Supp. at 892.} Although the \textit{Unocal I} court did not define knowledge, it suggested that knowledge might be implied from a participant’s past activities.\footnote{\textit{Id.} at 899.}

c. \textit{Unocal II - Mere Knowledge Does Not Suffice}

The \textit{Unocal II} court relied on two tests under the joint action theory of state action pursuant to which Unocal may qualify as a state actor: (1) Did Unocal conspire with the Myanmar military in its commission of unlawful acts? (2) Did Unocal participate in or influence the Myanmar military’s unlawful acts?\footnote{\textit{Unocal II}, 110 F. Supp. 2d at 1306-07.} The court concluded that plaintiffs had not provided sufficient evidence to conclude that Unocal was a state actor under either of these tests.\footnote{\textit{Id.} at 1306-07 (C.D. Cal. 2000).} The court also held that the mere fact that Unocal and SLORC shared the goal of a profitable project did not establish joint action.\footnote{\textit{Id.}}

Significantly, the \textit{Unocal II} court also suggested that knowledge by a private project participant of a public participant’s violations of international law, without more, does not transform the private participant into a state actor. Thus, plaintiff’s evidence that Unocal knew, prior to participating in the project, that the Myanmar military had a record of committing human rights abuses, that the military would be providing security for the project, and that the military committed, was committing, and would continue to commit human rights abuses in relation to the project, did not constitute a violation of international law.\footnote{\textit{Id.}}

The \textit{Unocal II} court added that in order for a private individual to be liable for the challenged acts committed by a government, the plaintiff must prove that the private individual was the proximate cause of the violation.\footnote{\textit{Unocal II}, 110 F. Supp. 2d 1294, 1306-7 (C.D. Cal. 2000).} In order to establish proximate cause, the plaintiff must prove that

\begin{itemize}
\item \textit{Unocal I}, 963 F. Supp. at 892.
\item \textit{Id.} at 899.
\item \textit{Unocal II}, 110 F. Supp. 2d at 1306-07.
\item \textit{Id.}
\item \textit{Unocal II}, 110 F. Supp. 2d 1294, 1306-7 (C.D. Cal. 2000).
\item \textit{Id.}
\end{itemize}
the private individual exercised control over the government's decision to commit the violation. This finding conflicts with the findings of the earlier proceedings, and will be argued in the Ninth Circuit appeal.

Finally, the *Unocal II* court considered the issue of whether Unocal was individually liable under the ATCA for the forced labor claims. The court observed that individual liability by Unocal required plaintiffs to show Unocal was legally responsible for the Myanmar military's forced labor practices. The court found that legal responsibility would attach to Unocal if it actively participated in or cooperated with forced labor practices. Mere knowledge that forced labor is occurring is not enough. The court concluded that plaintiffs had not presented any evidence indicating that Unocal sought to employ forced or slave labor. In fact, the court added, the evidence showed that Unocal was concerned about the use of forced labor by the military and that the military attempted to conceal the use of forced labor from Unocal.

**C. Implication of the Unocal Litigation**

The *Unocal* decisions are significant for two reasons. First, they announce that the conduct of American corporations must comply with a standard of international norms recognized by the United States. Second, the *Unocal I* court held that mere knowledge or reason to know by a sponsor that a partner is engaging in human rights abuses on behalf of the project may subject the sponsor to ATCA liability if it continues to receive these benefits. The language of the *Unocal I* decision could even be read to suggest that knowledge of human rights violations in general, not just in connection to the project, may suffice. The *Unocal II* decision, on the other hand, stated that ATCA liability lies only with parties that either (1) conspire in or (2) participate in or influence the Commission of Human Rights Violations.

**IV. MITIGATING THE HUMAN RIGHTS RISK**

**A. Risk Analysis**

Sponsors have several options in attempting to avoid liability for human rights violations committed in connection with the project. In choos-
ing a course of action, sponsors must first examine the risks. One authority on project finance has proposed a method of analyzing risk that consists of the following four steps:

1. Identification of the risk;
2. Determination of the likely costs of the risk;
3. Identification of the participant best suited to mitigate or assume the risk; and
4. Appropriate allocation of the risk.93

1. Identification of the Risk

This article assumes not that the project sponsor itself engages in human rights violations, but that the project sponsor becomes involved in human rights litigation through acts of the host government or other project participants. If the project sponsor itself engages in human rights violations, it has committed a wrong for which it should be prepared to pay. Naturally, there exists a gray area between acts committed by the project sponsor and those committed by other parties, especially in the case of project finance, where numerous parties work together closely.94 This is precisely what the plaintiffs in the Unocal case allege: not that Unocal itself engaged in human rights violations, but that SLORC, a project participant, violated human rights in furtherance of the project.95 The remainder of this paper addresses ways to keep out of this gray area and thereby avoid exposure to ATCA litigation.

The human rights risk straddles two of the traditional categories of risk in project finance: political risk and performance risk. When the host government violates human rights in such a way that ultimate liability may attach to a project sponsor, one thinks of risks associated with the political climate of a country and its government, hence the political risk classification. When the violator is a contractor or operator, one thinks of failures to perform that impede the project's course, hence the performance risk classification.

2. Determination of the Likely Costs of the Risk

Of the six ATCA cases filed against corporations, one has been dismissed and five are pending. One human rights observer, Zia-Zarifi, believes that it is "certain in the near future" that a court will hold a corporation liable for ATCA violations.96 He draws this conclusion based on several factors: American courts are used to hearing civil actions against corporations, courts have repeatedly indicated their acceptance of the no-
tation that a corporation can be held liable under the ATCA, and the more claims are filed, the more at ease courts and plaintiffs (and defendants, of course) will become with such litigation. On a more rhetorical note, Zia-Zarifi observes: "if the American system can hold [corporations] liable for engaging in bribery abroad, then it certainly can and should persecute [sic] [corporations] for acts of murder, torture or slave trading, and other violations of international human rights norms." 98

Estimating the costs of ATCA litigation is a speculative exercise. Based on prior awards, however, the damages could be astronomical. In eleven ATCA cases that reached final judgments between 1980 and 1995, damages awarded against individual defendants averaged $197,800,000.99 If one excludes the lone suit against a defendant with assets comparable to those of a corporation, in which Ferdinand Marcos was found liable for $1,966,000,000, the awards still averaged $21,000,000.100 In light of the tremendous wealth of some corporations compared with the countries in which they invest (in 1995, Myanmar had a GDP of $5.0 billion, Unocal had gross revenues of $4.1 billion, and Total had gross revenues of approximately $23.0 billion101), damages greatly in excess of these previous awards are conceivable. Even if a company is not found liable, it may still face considerable costs with respect to negative publicity, boycotts, lost time of executives who must deal with these issues, and high legal fees as lawyers travel to distant places to gather evidence. Unocal estimated its losses in 1996 related to its acts in Burma at about one million dollars—before suit had even been filed and a number of critical stories had made the front pages of major newspapers.102

3. Identification of the Participant Best Suited to Mitigate or Assume the Risk

It goes without saying that the participant best able to mitigate the risk of human rights abuses in connection with the project is the host government, contractor, operator, or other participant that violates human rights (again, assuming for the purposes of this paper, that the human rights risk excludes human rights violations by the project sponsors).

4. Appropriate Allocation of the Risk

As with other risks that the host government can best mitigate, such as expropriation, currency inconvertibility, and regulatory change, the host government is not always willing or capable of bearing these risks. This

97. Id.
98. Zia-Zarifi, supra note 94, at 145.
99. Stephens & Ratner, supra note 9, at 343-48. These averages do not include the damages awarded in the Marcos litigation.
100. Stephens & Ratner, supra note 9, at 348.
101. Tzutschler, supra note 12, at 381-82.
holds true with respect to the other project participants. As a result, project sponsors cannot always rely on risk allocation to protect themselves from liability for human rights violations.

Participants in a project have three ways of limiting their exposure to the human rights risk: first, they can perform due diligence to identify potential risks and decide which countries to deal with; second, they can obtain insurance; and third, they can try to shield themselves contractually. The remainder of this paper examines these three options.

B. Mitigating the Human Rights Risk

1. Due Diligence

Prior to developing a project, sponsors will undertake a feasibility study to identify the technical, economic, contractual, governmental, and financial aspects of a proposed project. Project feasibility studies should include examinations of the business environment of the host country. The sponsors should consider the host country's political, regulatory, and economic climate. Within this framework, project sponsors should also examine the human rights conditions in the proposed project site. The U.S. State Department's country reports and various human rights organizations provide such information.

Some commentators have recommended that companies doing business abroad investigate the potential host countries' human rights records. Human rights activists, in particular, state that companies should avoid doing business in countries with spotty human rights records because foreign investment subsidizes and legitimizes repressive regimes. Levi Strauss & Co., for instance, withdrew from Burma in 1992, citing the impossibility of doing business there without "directly supporting the military government and its pervasive violation of human rights." Likewise, George Soros divested his holdings in Peregrine Investments because of Peregrine's involvement in Burma. More recently, companies such as Compaq, Apple, Disney, Pepsi, Kodak, and Motorola have joined the exodus from Burma. Even companies less susceptible to consumer pressure, such as Texaco and Arco, have pulled out. Companies that do not sell directly to consumers, however, do not have the same sensitivity to public enmity. Freeport-McMoRan, for instance, which recently succeeded in getting ATCA claims

104. Id. at 155-60.
106. Nightline, supra note 35.
107. Millman, supra note 2, at 1.
108. Id.
109. Nightline, supra note 35.
dismissed, as a lumber company does not face the same public pressures as Nike or the Gap. Likewise for Unocal, which sold off most of its domestic refineries and gas stations in 1997 in order to free up funds to invest in exploration abroad, especially in Asia.

The other side counters that engagement promotes democracy. As Roger Beach, the chairman of Unocal, wrote in a response to a New York Times editorial condemning Unocal's venture in Myanmar, "[i]f history has shown us anything, it is that economic isolation only causes chaos, suffering and hardship for the people it is intended to help. It does nothing to improve living standards, promote democracy or advance human rights." Barbara Linney observed: "Both camps are claiming to be on the side of ethics, on the side of human rights." This debate has continued for decades, and will undoubtedly continue for far longer without yielding a definitive answer.

Other commentators take a more cautious view. Yves Miedzionogora suggests that companies consider the following three points before deciding to do business in a foreign country. First, if the U.S. State Department, for instance, prohibits doing business with or in a country, then the company should stay out, for it not only risks sanctions for violating the prohibition, but it likely will be held liable for ATCA claims. Such countries include Cuba, Iran, Iraq, Libya, North Korea, Sudan, and Burma. Second, if a country is known to treat its citizens badly, then companies operating in such countries face a high risk of ATCA liability. If adjudication of ATCA claims in United States courts were to have repercussions on United States foreign relations with that state, however, then the act of state doctrine may convince a court not to entertain the claim. Third, if a foreign country does not have a judiciary likely to allow potential plaintiffs to obtain relief, then United States courts will be more likely to hear the claim.

In the event courts decide to follow the standard set by Judge Paez in Unocal I, whereby knowledge by a project sponsor of a public participant's violations of international law suffices to transform the project sponsor

111. Iritani, supra note 102.
115. Miedzionogora, supra note 2, at 3-4.
116. Id. at 4.
117. Miedzionogora, supra note 2, at 4.
into a state actor, then an immediate benefit of conducting due diligence is that it may show that a project sponsor lacked the requisite knowledge for ATCA claims, assuming the due diligence turned up no human rights violations. If the view of Judge Lew set out in *Unocal II* prevails, then a project sponsor may be individually liable if it is legally responsible for the human rights violations of a public participant. In that case, even the fact that a project sponsor engaged in due diligence might help convince the court that the project sponsor was concerned about these abuses, and therefore, likely did not encourage the public participant to commit them.19

Beyond this evidentiary matter, however, due diligence may not be of tremendous use. Many countries that need project financing for infrastructure and the exploitation of natural resources are developing. While regrettable, it is a fact that developing countries tend to grant their citizens fewer human rights, as this concept is understood in the field of international law. Countries that commentators warn may cause troubles for businesses would include China, Indonesia, Nigeria, Pakistan and other authoritarian regimes in need of project financing. Companies that refused to engage in business in these areas would lose considerable economic opportunity. In recommending that its shareholders vote against a proposal calling for Chevron to develop country selection guidelines for investment, Chevron explained that "it is also important to remember that natural resource companies can only operate in regions where resources exist or are thought to exist. This is a constraint on our operations that is not experienced by most other businesses."21

In addition, projects in developing, but authoritarian countries can be very profitable. As mentioned previously, an analyst estimated that the Yadana project would increase Unocal’s per share earnings by ten percent.22 In deciding to remain in Burma despite protests, chairman of the Unocal board, Roger Beach, assured shareholders that lost business and legal fees associated with the Burma project had cost the company only $1 million in 1996.23 Shareholders rejected a pair of proposals critical of Unocal's association with Burma during the company's 1997 and 2001 shareholders' meetings.24 When asked why he had chosen to invest in Burma, former president of Unocal, John Imle, responded “[i]nitially, what we recognized there was A, the existence of the natural gas re-

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119. In the Unocal case, for instance, the court found that documents expressing Unocal’s concern about forced labor practices of the Myanmar government made it less likely that Unocal sought to employ forced labor. *Id.* at 896.
122. *Infra*, III-B.
124. *AFL-CIO, supra*, note 38; *Corporations Feel Heat, supra* note 38; and Young, *supra* note 38.
Thus, given the potential for returns on project financing, some companies may treat ATCA claims and other related problems as costs of doing business in certain countries. Conducting due diligence into the state of a country's human rights will assist prospective project sponsors in determining the risks they face there. Nonetheless, it may make economic sense for companies to invest in countries with questionable human rights records. These companies may consider various means, discussed below, of protecting themselves from liability for human rights abuses.

2. Insurance

Among the most common mitigation techniques for traditional country risks, such as inconvertibility of currency risk, expropriation risk, regulatory risk, and political violence risk, is political risk insurance. Multilateral, bilateral, and private insurers will compensate project sponsors that suffer financially as a result of political violence by third parties or illegal acts and material breaches of the project agreement by the host government. Insurance may not cover the human rights risk, however, as insurance coverage does not extend to blameworthy acts of the insured. The Overseas Private Investment Corporation (OPIC), which is funded by the United States Congress, for instance, excludes from insurance coverage actions provoked or instigated by the investor. Private insurance contracts contain similar terms. Typically, they exclude "wrongful, dishonest or criminal acts of the Insured," "provoking the Host Government in some manner . . ." or the insured's "failure to comply with the laws of the Host Country, or from any failure of the [insured] . . . to comply with applicable environmental, public health and worker safety standards of the World Bank." In addition, the insured must often warrant "that it has complied and will continue to comply in all material respects with the applicable laws of the Host Country and the Insured's Country . . ."
Political risk insurance is available only to insureds that do not have a hand in any of the injury that results from the host government's actions and that comply with the laws of their home country, the laws of the host country, and international standards set forth by organizations such as the World Bank. As a result, if a project sponsor is found liable in a United States court for violating the ATCA, it will not be eligible for political insurance coverage, because it will probably have violated most, if not all, of the conditions commonly found in insurance contracts. More fundamentally, a project sponsor will not be able to contract around these conditions, as it is likely to be against public policy to insure against human rights abuses.

Even though project sponsors cannot obtain insurance against the human rights risk, the standard terms under which multilateral agencies, such as the Multilateral Investment Guarantee Agency (MIGA), a member of the World Bank, and bilateral agencies, such as OPIC, provide political risk insurance will assist project sponsors in avoiding ATCA liability. First, these organizations have as a mission the facilitation of environmentally and socially responsible investments. OPIC states that it will not "[support] projects that contribute to violations of internationally recognized worker rights."\(^{132}\) The MIGA Definitive Application for Guarantee asks the applicant to identify potential worker safety problems the project may cause, and to describe measures to mitigate such hazards. The Definitive Application also asks whether the project will comply with health and safety guidelines of the host country, the investor's country, and the World Bank.\(^{133}\) The MIGA Operational Regulations, which define the conditions under which MIGA will provide insurance, state that insureds must undertake to comply with the laws and regulations of host countries.\(^{134}\) The Operational Regulations also require MIGA to conduct assessments with respect to, among other factors, the economic soundness and contribution to development of projects. In particular, MIGA must investigate the effects of projects on the social infrastructure of the host country.\(^{135}\) MIGA reviews the social aspects of all projects with the potential to cause "significant and diverse social impacts" before agreeing to underwrite them.\(^{136}\) As a result, public insurers may refuse even to consider projects undertaken in countries notorious for human rights violations. Perhaps this explains why

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133. MULTILATERAL INVESTMENT GUARANTEE AGENCY, Definitive Application for Guarantee (Sept. 1999) (on file with the author).


135. Id. at 1241 ($3.06).

Second, in order to foster socially sound projects, these organizations require the insureds to accept conditions which, if followed, will reduce the likelihood of ATCA violations. First, these agencies demand that the insureds comply with local and international laws and international standards. Article 12(d) of MIGA’s Convention, for instance, states that “[i]n guaranteeing an investment, the Agency shall satisfy itself as to: . . . (ii) compliance of the investment with the host country’s laws and regulations . . .” Both MIGA and OPIC expect insureds to meet strict health and safety standards for employees and the public.

3. Corporate Codes of Conduct

In order to channel the tremendous assets of multinational corporations into positive uses, the international community has long tried to subject multinational corporations to corporate codes of conduct, but to little avail. After twenty years of effort, the United Nations gave up on its attempt to draft a code in 1993. The Organization for Economic Cooperation and Development and the International Labor Organization produced codes of corporate conduct, but in the absence of any means of enforcement, they have remained aspirational. Corporations, too, have come up with codes of conduct, but they lack legal force. Nonetheless, codes of conduct may help a project sponsor avoid liability in an ATCA suit. If a sponsor can prove that it complied with its code of conduct seriously on a particular project, a court or jury may infer that the sponsor lacked the requisite knowledge for liability under the ATCA. In this way, a code of conduct could assist in proving proper corporate behavior.

Ideally, a sponsor would like to make a code of conduct legally binding on the participants involved in a project. The sponsor can accomplish this goal by inserting provisions from the corporate code of conduct into the various contractual agreements that bind the project participants. The next section discusses this strategy in greater detail.

4. Contractual Mitigation

Sponsors that choose to undertake a project in countries with political climates that raise the possibility of human rights risk must rely on contractual means to mitigate this risk. One of the primary advantages of structuring an investment as project finance is the ability to spread risk contrac-
Participants in a project cannot limit their exposure in this way to ATCA suits by third parties, however, since these third parties are not party to any of the agreements. As a result, the parties to a project must resort to contractual means to provide for internal allocation of the risks.

In principle, it is desirable to allocate a risk to the party best able to foresee, manage, control, spread, mitigate, or hedge against it. In practice, policy considerations and the relative bargaining and financial strengths of the project participants will also determine the allocation of risk.

a. Limiting the Liability of the Project Company

Among the advantages of project finance as a vehicle for investing is that it allows sponsors to limit their exposure through the formation of a project company. The project company is the entity that will finance, develop, operate, maintain, and sometimes own the project, thereby keeping the sponsors from direct participation in the project. The formation of the project company depends on accounting and tax considerations, local law and the objectives of the project sponsors.

Project companies generally fall into five categories: joint ventures, general partnerships, limited partnerships, limited liability companies, and corporations. The rules of thumb regarding the different types of entities apply to the project finance world: joint ventures allow participants great flexibility in management, but do not limit their liability; partnerships provide advantageous tax treatment and greater management participation and control, but limit liability to a lesser degree; limited liability companies combine attributes of partnerships and corporations; and corporations limit the liability of incorporators but provide less managerial flexibility and control.

Of these forms, the corporation best shields the investors from risks arising out of a project. As a result, sponsors that want to mitigate the human rights risk would be advised to incorporate their project company. In the Unocal litigation, for instance, Unocal has raised this argument, contending that it cannot be held liable for the acts of its subsidiary, Unocal Myanmar Offshore Co., which represents Unocal’s interest in the Yadana project. Incorporation will not always shield the parent from the

144. *Id.*
145. *Hoffman*, supra note 103, at 42-43, 133. Although a project company should more properly be called an “entity,” or “business organization,” since project companies can take the form of partnerships or joint ventures, this paper follows industry practice and employs the term “project company.”
146. *Id.* at 108, 133.
149. Branigin, supra note 43..
acts of the project company, however, because of the equitable remedy of piercing the corporate veil.

The doctrine of piercing the corporate veil is simple enough: courts will look beyond the corporate form when it is being abused. The United States Supreme Court wrote: "[a]lthough a corporation and its shareholders are deemed separate entities for most purposes, the corporate form may be disregarded in the interests of justice where it is used to defeat an overriding public policy. These notions of justice and public policy do not provide much guidance, but project sponsors would do well to remember the following precept: scrupulously observe the corporate form. This means that the project company should be run by officers as representatives of the project company, not the parent; when the project company enters into agreements, it should do so in its own name, not in that of the parent; and when the project company contract to perform, the parent should not represent that it supports the project company's performance.

The issue of piercing the corporate veil arose in the case of *Jota v. Texaco*. Too much direction from the head office in New York was one of the factors that led the U.S. Court of Appeals for the Second Circuit to require that the parent company, Texaco, submit to the jurisdiction of Ecuadorian courts for violations by its Ecuadorian subsidiary of, among other statutes, the ATCA. Ideally, the sponsor should behave like a passive investor.

These precautions do not guarantee that courts will honor the legal barrier between the parent and the subsidiary in the case of an ATCA claim. Courts in the United States pierce the corporate veil in approximately forty percent of cases where that remedy is sought. One study found that courts pierce the corporate veil more often when the plaintiff is a contract creditor (42% of cases) than when the plaintiff is a tort creditor (31% of cases). This study also found that courts pierce the corporate veil 40.5% of the time when the corporate defendant has violated a statute. Thus, while the fact that a project company commits a tort may not increase the likelihood of a court's piercing the corporate veil, the fact that it violates a statute may.

A second approach is related to the concept of worldwide financial responsibility of multinationals. Professor Jay Westbrook explains that the purpose of limited liability as a spur to entrepreneurial risk-taking and economic innovation should not apply to large multinationals in develop-


152. HOFFMAN, supra note 103, at 137-38.


154. Thompson, supra note 150, at 1048.

155. Id. at 1058.

156. Thompson, supra note 150, at 1058.
ing nations for two reasons: first, these multinationals are hardly entrepre-
neurial upstarts in these nations; and second, multinationals must not be
able to unleash the tremendous power and wealth they possess. On a re-
lated note, some commentators have argued that parent companies should
not be able to escape liability when their subsidiaries run hazardous in-
strumentalities or maintain armed forces for the parent's benefit.

Structuring the project entity in a way that minimizes governmental
participation is perhaps the most effective means to avoid being implicated
in human rights violations committed by a host government. Courts are
less likely to hear ATCA claims when the host government is seen as a
passive investor that does little more than grant a concession. John Rey-
nolds, who successfully defended Freeport-McMoRan against allegations
of violations of the ATCA and other laws, suggests that sponsors avoid
structuring their deals as joint ventures with host governments; ideally
sponsors should seek to be viewed as a contractor, rather than a partner, of
the host government.

b. Contracting with the Host Government

In light of the proclivity of United States courts to pierce the corpo-
rate veil, a project sponsor ought to consider transferring the risk to other
project participants. Because the host government is the party most likely
to violate human rights, the sponsor should attempt to have the govern-
ment bear this risk. Among the numerous agreements that bring a project
to life, at least two define the relationship between the host government
and the sponsors: the concession agreement and the support agreement
(also called implementation agreement). The concession agreement con-
tains the terms according to which the host government grants the sponsor
the right to construct, develop, and operate a project or exploit a re-
source.

When sponsors cannot cover all of their risk exposure through insur-
ance or other traditional means, they may turn to the host government for
assurances to deal with uncertainties of a particular project. The gov-
ernment will issue these assurances in the form of a support agreement,
which is a contract between the host government and the sponsor that ad-
dresses financial and political issues necessary to a project, but the other
project agreements. Typically, in a support agreement, the government

157. Jay L. Westbrook, Theories of Parent Company Liability and the Prospects for an Interna-
158. Treutschler, supra note 12, at 395.
159. Linney, supra note 2.
160. Reynolds, supra note 2.
(Apr. 18, 2000).
162. HOFFMAN, supra note 103, at 233.
163. U.N. CITRAL, supra note 143, at 8.
164. HOFFMAN, supra note 103, at 236.
undertakes to provide the requisite permits, to guarantee tax breaks, to provide protection, to refrain from expropriating the project, and to cooperate in general with the project.165

i. Concession Agreement

In an ideal world, the sponsor would attempt to include the following provisions in the concession agreement. First, the sponsor should insist that the host government represent and warrant that it complied with international labor standards and international law in connection with the project during the pre-development stages.166 The project sponsor must also ensure that the host government will continue to honor its undertakings after signing the concession agreement. If that fails, the project sponsor should request the host government to comply with international labor standards and international law in the customary “General Obligations of the Parties” clause of concession agreements.167 Such a provision can be inserted in the “Compliance with Laws” clause168 by adding customary international law as a law to be observed. These two clauses should contain examples of what could be considered to violate international law and labor standards, such as forced labor, forced relocation under certain conditions, physical abuse, and so forth. The sponsor should then list among the events of default leading to termination any representation or warranty made by the host government that turns out to be materially incorrect or any material failure to perform its general obligations.169

Governments may object to such clauses, since they might be seen to meddle in domestic affairs and to imply that the government carries out human rights violations. The sponsor might respond in three ways. First, it may argue that the clauses should be viewed as reinforcements of the country’s commitment to labor standards and international law rather than as admissions of guilt, in the same way that ratification of a human rights convention by a state reflects positively on that state. Second, the sponsor should point out its willingness to undertake the same obligation to comply with these laws. Third, lenders may require such a clause,170 which the sponsor could point to for leverage.171 Patricia Bajenski, Director of International Finance at Coastal States Management Corporation, has said that she had never heard of a government accepting to act within its own territory in accordance with foreign laws. The mere suggestion that a government do so would be a great insult.172

165. Id. at 237-41.
166. Gide Loyrette Nouel, Model Concession Agreement Relating to the Financing, Design, Transformation, Construction, Maintenance and Operations of [a] Toll Motorway, at Article 25 (on file with the author) [hereinafter Concession Agreement].
167. Id. at Article 13.
169. Concession Agreement, supra note 166, at Article 20.1(g).
170. Infra, IV(B)(5).
171. Linney, supra note 2.
172. Telephone interview with Patricia Bajenski, Director, International Finance, Coastal States
Just as many concession agreements provide for an independent engineer to report on the performance of the parties' obligations under the agreement, the sponsor should try to provide for an independent observer to report on the human rights conditions surrounding the project. This might be the most contentious of this Article's suggestions for several reasons. First, evaluating human rights is more subjective than evaluating technical compliance with the project's specifications. Second, finding and agreeing on an independent observer who is familiar with international human rights norms may not be easy. Third, concession agreements typically do not contain such provisions, and it is always more difficult to create a new and untested provision than to alter an existing one. Fourth, the cost of having someone on the project site to monitor human rights conditions could be expensive, judging by the high hourly fees charged by independent engineers. Finally, a government may object to the independent observer because the prospect of a reprimand for human rights violations within its borders is far more unsavory than a reprimand for, say, failure to obtain for the sponsor preferential tariff treatment. Nonetheless, it is essential to have an expedient mechanism for determining the existence of human rights violations so that the project sponsor can invoke the provisions described below and mitigate the human rights risk.

Multilateral and bilateral agencies already inspect the sites of their loan and insurance beneficiaries. The International Finance Corporation (IFC), a member of the World Bank Group, for instance, monitors the environmental and social aspects of its projects through supervision missions and project site visits, the frequency of which depends on the environmental and social complexity of the projects. MIGA, also a member of the World Bank Group, states that it may carry out monitoring visits to environmentally and socially sensitive projects. OPIC as well announces that it monitors compliance with United States environmental and workers' rights standards through site visits. As a result, because projects involved with these agencies already receive visits whose purpose is, among others, to assess the state of workers' rights and social conditions in general, the notion of an independent observer is not that radical.

The sponsor should also protect itself in the event of default by the host government in the following two ways. First, the concession agreement should provide for adequate compensation for the sponsor. Second, the concession agreement should also allow the sponsor to assign its interest in the project. This clause may be hard to negotiate, as concession agreements typically condition the assignment on the host government's


173. Concession Agreement, supra note 166, at Article 6.
175. MIGA, supra note 136, at para. 57.
176. OPIC Handbook, supra note 132, at 7.
177. Id. at Article 21.4.
Nonetheless, negotiation of such a clause is worth the effort because sponsors who are not subject to the jurisdiction of American courts, and that come from countries without laws equivalent to the ATCA, might express interest in taking over profitable projects.  

Sponsors can also rely on the standard liability and indemnification clause of concession agreements, where the party accused of liability for personal injury arising from violation of its obligations under the agreement to a third party agrees to indemnify, defend, and hold harmless the other party.  

Finally, sponsors should consider whether or not they want to require the host government to waive its sovereign immunity. Waiver will allow the sponsor to join the host government in case it is sued for an ATCA violation. In some instances, however, it may be to the sponsor’s advantage if the host government does not waive its sovereign immunity. In the Texaco case, for example, the Ecuadorian government had not waived its sovereign immunity, and consequently, could not be brought before American courts. Texaco argued that since the Ecuadorian government was a necessary and indispensable party, the suit could not be brought in the United States. The court agreed and dismissed the case in part on the ground of forum non conveniens, on the condition that Texaco submit to the jurisdiction of Ecuadorian courts.  

The same strategy did not pay off in the Unocal case, however, as the court found that SLORC, which had not waived its sovereign immunity, was not a necessary and indispensable party. Therefore, the suit could go forth with Unocal as the sole defendant.  

ii. Support Agreement  

Sponsors are naturally inclined to seek as much support from the host government as possible. Nonetheless, sponsors must be wary of undertakings by the host government to provide physical protection against local opposition to projects. Commentators write that such provisions are a good way to mitigate political risk and are useful in pipeline and transportation projects which, in light of their geographical breadth, are particularly susceptible to sabotage.  

As a result, commentators have begun advising sponsors to avoid mili-

179. The court in the Unocal case based its denial of class certification on this possibility, saying that the redressability factor of class certification would not be satisfied by requiring Unocal to cease its operations in Burma, since other companies would step in. See generally Doe v. Unocal Corp., 67 F. Supp. 2d 1140, 1143 (C.D. Cal. 1999).  
180. Concession Agreement, supra note 166, at Article 22.2.  
181. HOFFMAN, supra note 103, at 251.  
184. HOFFMAN, supra note 103, at 236.  
185. Fitzgerald, supra note 1, at 36.  
186. HOFFMAN, supra note 103, at 230.
tary assistance in favor of private security arrangements. The sponsors should assure themselves that these security forces have no links to the military and that host government participants in the project do not use project funds or equipment for military purposes.

The sponsor might also try to get the host government to agree to conform to international norms. Here, too, examples of which types of acts might be deemed to violate human rights would be useful, though strong resistance by the host government is to be expected.

Convincing a state to accept some of these provisions, and in the process compromise its sovereignty, is understandably a difficult task. It is not impossible, however. Countries in need of infrastructure will go to great lengths to encourage investment. The Turkish Parliament, for instance, in order to attract foreign sponsors, recently took acts limiting its sovereignty. Just as Turkey had begun to receive foreign investment in energy projects in 1996, the Turkish Constitutional Court ruled that private power projects were concessions, and, consequently, were subject to review by the Turkish Supreme Administrative Court, which had the authority to revise the terms of those agreements in favor of the state. Not surprisingly, foreign investment fell. Three years later, the Turkish Parliament removed this obstacle to foreign investment by amending the Turkish Constitution to allow energy project contracts to be governed by private law instead of administrative law. If a country is willing to convert concession agreements from matters of administrative law to private commercial law for the purpose of promoting project finance, others may be willing to make concessions regarding human rights.

c. Contracting with the Project Contractors and the Operators

The construction contract is at the core of project finance, as it brings together into a cohesive whole the technical and financial parameters of the project. It is also an ideal opportunity for the sponsors to ensure that human rights violations do not haunt their project. The types of human rights violations alleged in the Unocal case: torture, slavery, forced labor, and assault, are most likely to occur in the construction phase of the project. The laying of a pipeline across a people’s land may prompt it to resist. An off-shore platform that is running behind schedule may encourage the use of forced labor, and a plant that is losing money may cut costs at the expense of workers’ safety and wages. Such violations can also occur during the operation and maintenance phase of the project. The fact that forced relocations and worker-intensive construction projects will have al-

187. Linney, supra note 2; Reynolds, supra note 2.
188. Linney, supra note 2.
189. Leigh Hall & Emre Derman, Turkey Puts the Final Piece in the IPP Legislative Jigsaw, 188 PROJECT FIN. INT’L 56, 56-57 (2000).
ready ended, however, somewhat reduces the probability of violence during this phase.

In addition, sponsors should seek to insert certain clauses in their respective agreements to further shield themselves from liability arising out of human rights abuses that occur during these phases. If sponsors decide to construct or operate the project themselves, then obviously they should take great care to prevent any human rights abuses from taking place.

i. Construction Agreement

Project sponsors' greatest concerns are that the project be completed on schedule and that it perform as expected.\(^{191}\) Selecting an internationally recognized and experienced contractor will protect sponsors against completion and performance risks.\(^{192}\) Likewise, experienced contractors are more likely to avoid situations that can lead to human rights violations, if only to preserve their reputations.

Project sponsors should insist on the following clauses, all of which are standard for construction contracts: (1) a clause mandating compliance with prudence and laws, (2) a personnel clause, (3) a labor relations clause, and (4) an indemnity clause. In the clause mandating compliance with prudence and laws, the contractor undertakes to work prudently and in compliance with local and international laws.\(^{193}\) Customary human rights law may be included in this clause. The personnel clause will typically place on the contractor the burden of hiring competent personnel, training the personnel, and assuring their safety.\(^{194}\) The labor relations clause renders the contractor responsible for employment decisions, work conditions, and labor disputes.\(^{195}\) It would be helpful to insert in these sections provisions about respecting basic labor standards as set forth, for instance, by World Bank entities such as the IFC and MIGA.\(^{196}\)

The representations and warranties clause of construction contracts typically requires contractors to represent and warrant that they complied with all applicable laws in constructing the facility.\(^{197}\) Here, too, sponsors

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192. Id. at 68.
194. O'Sullivan, supra note 911, at 81; Articles 4.1(a) and (f) of the sample construction contract appearing in STEARNS AND HAINES, supra note 193, at 71-72. Finally, some construction contracts, particularly turnkey contracts, obligate contractors to provide security for the project. See generally HOFFMAN, supra note 103, at 276. Such clauses will further remove risk from sponsors.
195. Article 10 of sample construction contract appearing in STEARNS AND HAINES, supra note 193, at 78-79.
197. HOFFMAN, supra note 103, at 289.
may want to mention customary international law and provide examples of acts that would violate such law.

In the indemnity clause, contractors agree to defend, indemnify, and hold harmless the owner for any claims or losses arising out of the contractors' negligent, willful, or wanton acts or omissions. Specific reference to customary international law should be made in this clause.

ii. Operation and Management Agreement

The operation and management agreement is similar to the construction agreement in that the primary risks are adequate performance within budget and insuring that the operator has the responsibility of managing personnel matters and following applicable laws. Consequently, the project sponsor should insert provisions similar to the ones inserted in the construction agreement. Likewise, since operation and management agreements also contain indemnification clauses, the sponsor should do as it did with respect to the construction agreement. In addition, the sponsor would do well to hire an experienced operator for the reasons mentioned above. Finally, the sponsor may try to negotiate from the operator a representation and warranty that it did not violate any human rights laws.

5. The Role of Lenders

a. Public Lenders

Nations, the World Bank, and other constituting bodies have entrusted public lenders with a mission beyond profit maximization. The IFC, for instance, announces its policy that "all its operations [be] carried out in an environmentally and socially responsible manner." Even bilateral agencies, which are more intent on promoting exports and domestic jobs than development, consider the social impact of the projects they finance. The mission of OPIC, for instance, is "to mobilize and facilitate the participation of [U.S.] private capital and skills in the economic and social development of less developed countries and areas . . . ." OPIC finances projects that "promise significant benefits to the social and economic development of the host country . . . ." and is

\[\text{References:}\]

199. \textit{Id.} at 332-33.
200. \textit{Stearns & Haines, supra} note 193, at 331.
201. \textit{Id.} at 328.
204. \textit{OPIC}, supra note 132, at 1.
205. \textit{Id.} at 2.
prohibited by law from "supporting projects that contribute to violations of internationally recognized worker rights."206

Public lenders will often conduct extensive due diligence to ensure that the projects they have been asked to finance will fulfill their mission. Generally, the IFC expects all projects in which it invests to comply with applicable local, national, and international law.207 In particular, IFC sponsored projects must also comply with the IFC's General Health and Safety Guidelines, which require project sponsors to assure their workers safe and sanitary working conditions.208

IFC projects that affect indigenous peoples must comply with the World Bank standards for dealing with these groups as set forth in Operational Directive (O.D.) 4.20, Indigenous Peoples.209 Operational Directive 4.20 seeks to ensure that indigenous peoples benefit from projects financed by the World Bank and its affiliates and that the development process respect dignity and human rights.210 In accordance with these principles, sponsors obtaining loans for projects that will affect indigenous peoples must prepare an Indigenous Peoples Development Plan, in which sponsors outline potential problems, identify the indigenous peoples' social conditions and legal rights, and propose solutions and means for their implementation.211 The IFC requires the sponsors of projects that may involve involuntary resettlement to provide a detailed resettlement plan that will benefit the resettled persons. The sponsors must demonstrate, among other things, the suitability of the proposed resettlement site, the adequacy of compensation to the resettled persons, and the sufficiency of community participation in the resettlement.212

Once a public lender has approved a project, the sponsors must continue to comply with the often stringent standards for social protection set forth in the lending agreements. OPIC financing documents, for instance, require the investor to agree to respect worker's rights in terms of wages, collective bargaining, and acceptable health, safety, and age levels.213

Public lenders, who are interested in promoting development, will

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help project sponsors avoid liability for human rights violations in two ways. First, the feasibility studies conducted by these lenders during the application process will eliminate from contention projects that have a strong chance of causing excessive disruptions to the lives of the people who live near the project site, in turn reducing the risk of conflict and violence. Second, these lenders will condition the disbursement of funds on compliance with laws and on observance of workers' rights and safety. Commercial lenders often ask the IFC and other public lenders to participate in risky projects because public lenders have relationships with a large number of governments. In this capacity, public lenders enhance a project's stability by acting as a buffer between a host government and private lenders.214

b. Commercial Lenders

Despite their primary concern with profits, commercial lenders, too, can play an integral role in helping project sponsors mitigate the risk of ATCA liability. This role takes on considerable importance in projects that do not have any public lenders, such as the Yadana gas field project in Burma.

Standard credit agreements contain several provisions that will indirectly require sponsors to respect human rights. In appraising project risks, lenders look to the experience of the contractor and operator, while placing particular emphasis on the ability of the contractor to work with a local labor force.215 Presumably, experienced contractors and operators are less likely to violate the human rights of their workers and the surrounding population.

Commercial lenders will also demand that project contracts be assignable and assumable to increase their value as collateral.216 This requirement should assist project sponsors in obtaining an assignability clause in the concession agreement.

Credit agreements have four broad areas that may mitigate ATCA violations. First, lenders set forth conditions precedent that must be met prior to the release of funds. Among the conditions precedent will typically be the accuracy of representations and warranties and an absence of defaults or breach of any project agreement.217 Second, borrowers covenant to comply with laws and regulations, to observe the credit agreement and all project agreements, and to construct and operate the project in accordance with industry standards.218 Third, borrowers represent and war-

214. Carlos Franzetti, Principal Counsel to the IFC, Presentation at The University of Texas School of Law (Apr. 13, 2000).
216. Id. at 546.
218. HOFFMAN, supra note 103, at 575-77; O'Sullivan, supra note 191, at 101; Warner, supra note
rant upon each disbursement that they have complied with all laws and regulations, that they have not defaulted on any of the project agreements, and that there is no pending or threatening litigation that could adversely affect the project. Fourth, the credit agreement will list as events of default the material inaccuracy of any representation or warranty, the failure to observe the covenants, and the material default by a party of any significant project agreement.

Finally, commercial lenders tend to view the participation of multilateral and bilateral agencies in the financing of a project as a form of political risk insurance, since host governments will be reluctant to jeopardize their relationship with the World Bank, OPIC, the EBRD, and other agencies through acts harmful to projects they are financing. If a commercial lender requests the sponsor to obtain the participation of public lenders, then sponsors will have to observe the stringent standards of these lenders.

Although commercial lenders do not yet inquire into the human rights conditions associated with an investment, in light of their reluctance to take on uncertain and unquantifiable risks, they may begin to insist on such clauses.

V. CONCLUSION

Regardless of which standard the Ninth Circuit Court of Appeals adopts for determining the liability under the ATCA of project sponsors for torts committed in relation to a project, the human rights risk has become part of the project's finance landscape. Project sponsors have several means of protecting themselves against ATCA liability, all of which entail compromise. The best way is to restrict investment to countries with a solid human rights record. This strategy, however, may keep sponsors out of potentially lucrative markets. Sponsors can also seek to limit their liability by acting like passive investors. The inability to exercise control may not satisfy sponsors who have considerable investments at stake, however.

Contractual mitigation offers a hopeful, though untested, means of reducing the human rights risk. Demanding a host government, or other project participant, to accede to human rights may seem presumptuous, if not impractical. Many project agreements already contain provisions that should encompass the types of acts covered by the ATCA. When asked whether the IFC would change its policies in response to the ATCA, Carlos Franzetti, Principal Counsel of the IFC, replied that if parties comply

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217, at 159-60.
219. HOFFMAN, supra note 103, at 217; O'Sullivan, supra note 191, at 102.
220. HOFFMAN, supra note 103, at 592-4; O'Sullivan, supra note 191, at 103; Warner, supra note 217, at 162.
221. Warner, supra note 217, at 166.
222. Vinter, supra note 148, at 219.
with the terms of the IFC's loans, ATCA violations should not take place. 223 Despite these provisions, human rights violations do take place. This fact has led one expert to state that contractual mitigation is not an option; project sponsors must rely instead on acting like passive investors and keeping away from the state military. 224 Contractual provisions may nevertheless be of some help. Project sponsors could try to make contractual mitigation more meaningful by reinforcing the language of the provisions, perhaps by explicitly referring to the law of nations. Forceful language may convince the host government that the sponsor is serious about human rights. Forceful language may also convince a jury that the sponsor lacked the requisite knowledge. Forceful language, however, will require the sponsor to concede other points during negotiations with its partners.

Ultimately, the sponsor's course of action will come down to business decisions. How much does a sponsor want to invest in a particular country? How badly does a country need foreign investment? How much is the sponsor's reputation worth? How much control and security is the sponsor able to forsake? How much is the sponsor willing to concede in order to obtain contractual protection? These business decisions are particularly difficult to make in light of the unsettled state of the law regarding corporate liability for ATCA violations. Nonetheless, the calculus of engaging in project finance abroad has changed in the past several years and project sponsors need to stay abreast of legal developments in this field.

223. Franzetti, supra note 214.