

# THE IMPACT OF SOVEREIGNTY AND BOUNDARY DISPUTES ON COMMERCIAL INVESTMENTS

01 July 2016 | Global

Legal Briefings - By **Andrew Cannon, Partner**

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As can be seen from the merest glance at the world's press, there remain a large number of unresolved sovereignty disputes around the world. According to the Maritime Boundaries Research Institute of the University of Dundee, as at June 2015, more than half of the 640 or so potential maritime boundaries were classified as unresolved or in dispute. This figure naturally excludes boundary disputes on land and internal secession disputes awaiting resolution. A number of boundary disputes are very high profile – for example, competing claims in the South China Sea, and the continuing dispute between the United Kingdom and Argentina over the Falklands/Malvinas, are significant sources of geopolitical tension.

Disputes over territory such as islands can be based on many different grounds, including geographical contiguity, claims to self-determination, historical claims (such as those based on the ethnic background of the indigenous people or disputed colonial treaties), or the disputed territory may be of political or strategic significance. Maritime delimitation disputes may themselves arise from disputes as to sovereignty over land, because as one international judge put it, “the sea follows the land”. Classic examples include disputes over sovereignty of islands, and indeed disputes concerning whether specific territory is properly classified under UNCLOS as an island at all (giving rise to full maritime zone entitlements), or is instead simply a “rock” with only a territorial sea. Equally, many maritime delimitation cases have relatively little origin in onshore sovereignty tussles and concern almost exclusively an interpretation and application of the provisions of the law of the sea.

Over recent times, many of the world's boundary disputes have arisen from, or have been exacerbated by, economic elements, in particular the discovery of hydrocarbons. Both land and maritime boundary disputes can have a significant impact on the international investment decisions of commercial actors and the political and economic development of a State. A feature of many, if not the majority of, boundary disputes is their longevity. A prime example is the dispute between Venezuela and Guyana over a mineral-rich area of land which began between the US and Britain in the nineteenth century and was revived last year following the discovery of oil off the coast of the disputed territory.

Why are sovereignty disputes relevant to commercial actors? A State exercises exclusive jurisdiction over its territory, and enjoys sovereign rights over associated natural resources. Investors who intend to explore and hopefully exploit natural resources need to know which State exercises sovereignty or sovereign rights over the relevant territory or maritime space and on what basis, and therefore which State has the exclusive sovereign right to grant concessions in relation to that territory. Unresolved competing maritime claims also have the potential to undermine an investment.

As well as the legal risks associated with commercial dealings with a State that does not have rights over the relevant area or resources, there are also important political, commercial and potentially reputational risks to consider.

From a State perspective, the satisfactory resolution of a boundary dispute can unlock the economic potential of natural resources. The existence or even spectre of a territorial or maritime boundary dispute can undermine the State's ability to exploit those resources.

## **IN BRIEF: TYPES OF DISPUTE AND METHODS OF RESOLUTION**

A dispute may exist in relation to the status of a territory itself (for example, as to sovereignty over the Falklands/Malvinas), or in relation to territorial areas where sovereignty is disputed between two or more neighbouring States (as was the case on the border between Cameroon and Nigeria). Sovereignty disputes over territory on land can often lead to related maritime boundary disputes, including where claims to maritime rights cover the same maritime areas (as is the case between Thailand and Cambodia in the so-called Overlapping Claims Area).

In accordance with the UN Charter, disputes between States, including as to sovereignty over territory or maritime rights, must be resolved by peaceful means. UNCLOS specifies a number of peaceful means by which disputes are to be settled. Whilst classically, disputes between States have been referred to the International Court of Justice (the **ICJ**), the principal judicial organ of the United Nations, maritime boundary disputes may additionally be referred to an ad hoc tribunal established under Annex VII of UNCLOS, or to the International Tribunal for the Law of the Sea (the **ITLOS**), established under UNCLOS. Disputes may also be submitted to arbitration pursuant to a treaty (for example, the ongoing arbitration between Timor-Leste and Australia) or other special agreement. Of course, even once a dispute has been submitted for resolution to a dispute resolution body, the proceedings may take a number of years to complete and, as discussed further below, have the potential to disrupt ongoing exploration or other commercial activity in the region.

**EXAMPLES OF FORMAL DISPUTE RESOLUTION:**

ICJ: Somalia v Kenya; Costa Rica v Nicaragua

UNCLOS: Barbados v Republic of Trinidad & Tobago, Guyana v Suriname

ITLOS: Bangladesh v Myanmar; Ghana /Ivory Coast

Ad hoc: Eritrea/Yemen

States may reach a resolution of disputes without recourse to a decision-making body, with the outcome of their agreement enshrined in a boundary treaty. Indeed, the prospect of mutually beneficial economic co-operation may provide sufficient incentive to bring both sides to the negotiating table. However, the settlement process may be long and uncertain. For example, in 2015 India and Bangladesh finally implemented a land boundary agreement which had been signed in 1974. Further, interpretation or implementation of an agreement or treaty, or even a judgment of the ICJ or an international tribunal, may lead to further disputes.

Where a dispute concerns the exercise of the right to self-determination, the resolution may be achieved by constitutional means and within the framework of the territorial integrity of the relevant State (eg, the secession of the Republic of South Sudan which was achieved by referendum after years of conflict). However, in some cases such disputes may be resolved by non-constitutional means, as was the case of Eritrea's war of independence from Ethiopia. Any resolution may be temporary and will depend, in any case, upon international recognition of the new State.

**“PROVISIONAL ARRANGEMENTS OF A PRACTICAL NATURE” - JOINT DEVELOPMENT ZONES**

Pending resolution of a dispute, States are encouraged by UNCLOS to make “*every effort to enter into provisional arrangements of a practical nature*”. Accordingly, whilst a permanent agreement may take many years to accomplish, States may nonetheless be able to reach an agreement to establish a Joint Development Zone (or JDZ) which will enable them to explore and develop the natural resources within the disputed territory. Under JDZ agreements, the States suspend their disputes over sovereignty, formalize the conditions for development and agree to the sharing of returns. The terms of JDZs vary, but the two States often cooperate to hold licensing rounds on a joint basis unless they have devolved their sovereign and regulatory rights and powers to a joint development authority (as is the case in the Nigeria/Sao Tome JDZ). The establishment of a JDZ can be a positive step which provides more security for commercial stakeholders, albeit that there may remain certain points of uncertainty. For example, the duration of the joint development agreement may be unclear or capable of variation. There may also be a lack of clarity as regards treatment of hydrocarbons which straddle the border of the JDZ into the recognized sovereign territory or maritime control of one of the States in the absence of an international unitization agreement.

## **KEY ISSUES FOR COMMERCIAL STAKEHOLDERS**

The economic reality is that opportunities for activity in disputed territories cannot be ignored. However, the risks are complex.

The position under international law with respect to an opportunity offered to explore or develop a field is a primary consideration. For example, an IOC considering a licence or concession opportunity needs to assure itself regarding the extent to which the State in question is able to grant those rights. There may be competing claims to sovereignty over the territory in question. Further, the claim of a State in relation to a territory may be questionable in light of other claims. These claims may be those of another State, or the territory concerned may be non-self governing. A maritime boundary may not have been established and the area in question may be subject to competing entitlements and overlapping claims.

Some of these same considerations apply even if the rights are not derived directly from a State. For example, when looking at farm-in opportunities, it is important to make sure that the title to the original petroleum agreement is validly granted as a matter of international law, otherwise any further rights derived from it are potentially unenforceable.

The fact that an oil or gas concession has been granted by a particular State is not in itself determinative of the sovereignty of that State over that territory or delimitation of a maritime boundary. Nor can it be relied upon to justify the adjustment or shifting of provisional lines of delimitation. The now consistent case law of international courts and tribunals is that the presence of such concessions is only relevant where it evidences or was based upon the existence of some express or tacit agreement between the States relating to the rights over the area in question.

The flipside of the encouragement in UNCLOS to enter into provisional arrangements is the existence of a similar exhortation to make every effort “*not to jeopardize or hamper the reaching of the final agreement*”. This standard has been invoked where concessions have been granted by one State in disputed areas. In this context, a tribunal considering competing claims may interfere substantially with exploration or other commercial activity in disputed areas, if a risk of irreparable damage or prejudice to one of the party’s rights can be established as resulting from that activity.

For example, in the Aegean Sea Continental Shelf case between Greece and Turkey, Greece sought an order from the ICJ which would have put a halt to exploration activity and related scientific research that had been granted by Turkey under a concession. In the event, the ICJ dismissed Greece’s application on the basis that there was no irreparable prejudice. In a more recent example, a number of concessionaires were facing possible disruption last year when a special chamber of the ITLOS considered the request of Ivory Coast for provisional measures to stop drilling in the context of a territorial dispute with Ghana. The special chamber ordered Ghana to prevent any new drilling in the disputed area and to monitor strictly, and prevent the dissemination of, non-public information from past, ongoing or future exploration activities which could be used to the detriment of Ivory Coast.

Putting aside the fact that investment treaties may be of very limited value in protecting against such legal risks, investors also need to consider the risks of reputational damage attendant to investing where there exists a dispute as to sovereignty or maritime jurisdiction. In particular, commercial activity in, or associated with, an area in which the basis of a territorial claim is controversial can lead to considerable criticism and broader business impacts. Shareholders can react in a high profile and negative way to activities in areas of dispute, with pension funds dropping investments. Oil companies have also been on the receiving end of civil claims in their home jurisdictions, based on allegations relating to activities in areas subject to historic and on-going disputes. Such claims often make unpalatable allegations, for example referring to corruption of government officials in connection with the investment and indirect funding, and thus facilitation of breaches of international law.

Further risk management issues for an investor include the potential for regular flare-ups in localised violent conflict. Indeed, possession of oil or gas fields and related installations can often become a focus in civil conflict, particularly in areas where sovereignty is disputed. Fighting or other military attention may lead to temporary cessation of production.

Therefore, for those invested in disputed territory or areas of overlapping maritime claims, the impact of escalating conflict and/or increasing political tensions at State to State level, is significant in many ways. In this context, it is difficult for a commercial party to avoid taking some sort of role in a State to State dispute in which private actors, of course, have no standing. However, as described below, a cautious approach is necessary.

## **INVOLVEMENT OF COMMERCIAL ACTORS IN BOUNDARY DISPUTES**

In its award in the investor-State arbitration between RSM and Grenada the tribunal observed that it “*must highlight how uncommon it is to have a private commercial party ... directly involved in maritime boundary negotiations between sovereign states.*” This observation is broadly accepted: sovereignty over territory is one of the basic characteristics of being a State. Boundary negotiations are usually highly confidential and diplomatically sensitive. Third parties have no standing in formalized resolution of boundary disputes and, as the same tribunal noted, “[p]rivate, foreign oil companies are rarely involved in sensitive and delicate matters such as maritime boundary negotiations because of the high potential for conflicts of interest”.

Private actors must therefore keep sight of whose boundary dispute it is. Undue or inappropriate influence in discussions between States concerning their boundaries can have a deleterious effect and actually undermine efforts between those States to reach an amicable resolution. That said, where revenue-generating activity (for example, the exploitation of hydrocarbons or, indeed, even fishing) is hindered by ongoing boundary disputes, commercial actors can put further pressure on, and provide motivation from States to reach a resolution where possible. Commercial actors may therefore play a careful but legitimate role in trying to bring States together to put an end to developmental “chill” and achieve the positive benefits of resolution of a boundary dispute.

## **KEY POINTS FOR STATES IN THE REALISATION OF ECONOMIC BENEFITS AND THE RESOLUTION OF DISPUTES**

The need to exploit resources can provide the impetus to tackle sovereignty and maritime boundary issues head on. The key to establishing such claims is preparation. A State will need solid legal, technical and political advice on the merits and disadvantages of different courses of action and how to achieve a peaceful method of dispute resolution. The economic motivation of a State will of course be relevant – for example, a State’s priority may be the short to medium term exploitation of resources, over and above a permanent determination of a boundary.

It will be important to consider the applicable law, including to investigate whether there have been any previous relevant agreements, their scope and their status. The expertise of a State’s team should extend to geography and (for maritime claims) hydrography, and historical and anthropological investigation may also be imperative. Fundamental to creating a strong position, whether in negotiations or in the context of formal dispute resolution proceedings, will be preparation and the mastery of all this information together to create a coherent legal and technical argument as to the State’s rights.

Particularly where there are promised riches of hydrocarbon discovery and exploitation, disputes as to sovereignty over territory and maritime boundaries are unlikely to decline. As we go to press, for example, the dispute between Ghana and Ivory Coast continues before the ICJ, and maritime boundary disputes continue to rumble on the Aegean Sea, involving Cyprus, Greece, Turkey and in some areas, Syria. Herbert Smith Freehills' Public International Law practice has considerable experience in advising both States and commercial clients on issues concerning disputed territory, delimitation of boundaries and the emergence of new States. For example, we were the first firm to commence an Annex VII arbitration under UNCLOS (Barbados v Trinidad and Tobago) and our specialists have been involved in a number of other disputes between States (including Eritrea/Yemen and Bangladesh's disputes with India and with Myanmar), and between States and oil companies.

For further information on investment protection, see [INVESTMENT PROTECTION: PROTECTING INVESTMENTS IN A VOLATILE WORLD](#) in Issue 1 of Inside Arbitration.





## KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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