

# International Construction Law

## Academic Monograph



The “right to regulate” doctrine (RTR) is a fundamental principle that enables states to exercise their sovereign powers in order to protect public interests such as safety, environmental protection, and human rights. In international law, RTR plays a crucial role, especially in the field of international construction contract law (ICCL), which requires balancing the interests of various actors—both state and non-state. This doctrine allows states to regulate the terms of international construction contracts to ensure compliance with norms that safeguard public interests, including environmental standards, labor laws, and investment protections.

Importantly, the right to regulate extends not only to states but also to an increasing number of non-state actors whose influence on international relations is ever more significant. A striking example is the Holy See, a *sui generis* subject of international law. The international legal personality of the Holy See is based not on traditional political sovereignty but on its spiritual mission. Its unique status enables it to maintain diplomatic relations with over 180 states and actively participate in international organizations [Araujo, 2000]. This example underlines that legal personality in international law is diverse and does not always depend on traditional attributes of statehood such as territorial control or sovereign authority. Applying RTR to such unique actors as the Holy See permits flexible regulation of their conduct in international relations despite their lack of classic sovereign powers.

No less significant is the example of the United Nations. Although the UN does not possess sovereignty in the classical sense, it wields considerable influence in international relations and actively participates in regulating various aspects of international construction law. For instance, during peacekeeping and reconstruction projects in post-conflict regions, the UN intervenes in construction processes by imposing requirements to uphold environmental standards and human rights. In this case, the RTR doctrine

enables the UN to influence international construction contracts even though its legal personality is not rooted in political sovereignty.

Furthermore, the right to regulate doctrine is actively applied by states such as the United States. U.S. law sets high environmental and labor standards for companies operating abroad. Even when American companies enter into international construction contracts in other countries, they must comply with U.S. regulations, including environmental protection and workplace safety standards. This example clearly demonstrates how RTR allows states to regulate the activities of non-state actors, including transnational corporations, thereby safeguarding public interests beyond their own borders.

These examples— the Holy See, the UN, and the USA—show that international legal personality can take various forms. By bringing non-state actors (like international organizations and religious entities) within the purview of the right to regulate, the doctrine permits flexible oversight of their involvement in international construction relations. This expands the possibilities for regulating international contracts and ensures the protection of public interests even when those actors lack the traditional hallmarks of sovereignty. Thus, RTR provides a legal foundation for effective and multifaceted regulation of international relations in the construction sector and other fields where the interests of different subjects of international law must be accommodated.

To better understand state legal personality and its interaction with the RTR doctrine, it is useful to turn to the theoretical work of Georg Jellinek. Jellinek developed the concept of state self-limitation and self-imposed obligation [Jellinek et al., 1900]. His theory illustrates how a state, in exercising its sovereign rights, can voluntarily limit itself in certain respects in order to honor its international commitments. For example, in international construction contracts, states often accept provisions that constrain their freedom to intervene in the economy so as to provide legal stability for foreign investors. At the same time, state authorities retain sovereignty over internal regulatory matters.

Jellinek's theory reconciled two opposing views on the nature of state sovereignty: the legal positivism of scholars like Gerber and Laband, which emphasized the supremacy of the head of state as the bearer of authority, and Gierke's "legal socialism," which recognized the role of corporations and social groups in influencing the structure of power. Jellinek's synthesis demonstrated that a state's legal personality can evolve and adapt to changing domestic and international conditions, a point that is especially relevant in the context of RTR.

The Holy See example shows that the international legal personality of non-state actors can take unconventional forms. The Holy See engages in diplomatic activities and international negotiations; its status is founded on spiritual sovereignty rather than traditional state attributes like territory or population [Kunz, 1952]. This case highlights that international legal personality can extend beyond classic statehood to special entities, and the RTR doctrine allows accommodating such uniqueness.

The primary practical goal of the "right to regulate" doctrine is to affirm the sovereign authority of states to enact norms aimed at protecting public interests—environmental protection, public safety, public health, and other key policy areas. At the same time, states' exercise of the right to regulate must not unduly infringe the rights of foreign investors to fair treatment and the protection of their investments. In the context of international construction contracts, this necessitates a careful balance between state sovereignty and the rights of foreign participants to a stable regulatory framework. Harmonizing public and private interests in the economic sphere not only protects societal interests but also helps ensure long-term legal stability and trust for investors.

An example of the successful application of RTR in arbitral practice is the case of SAUR International SA v. Argentine Republic. In that dispute, the arbitral tribunal upheld Argentina's right to implement measures to protect public welfare, despite their impact on the interests of a foreign investor. The investor, SAUR, had argued that a freeze on water service tariffs and other government interventions in market mechanisms caused losses and violated its investor rights, essentially claiming that the government's actions circumvented contractual obligations and international standards. Argentina, however, justified its measures by the necessity of safeguarding the public

interest amid an economic crisis. The government contended that its actions were aimed at preventing social and economic collapse and protecting the population, who would otherwise be unable to afford increased water rates during the crisis. The tribunal recognized Argentina's right to introduce regulatory measures in the face of extraordinary economic circumstances. It noted that Argentina's actions, though detrimental to SAUR's commercial interests, were directed toward protecting higher public values such as citizens' welfare and economic stability. The tribunal also observed that the measures were non-discriminatory and justified by the need to protect society's interests. This award underscores the importance of acknowledging states' right to regulate under international law.

Another instructive example is *Methanex Corporation v. United States*. Methanex claimed that California's ban on the use of a methanol-based fuel additive violated its investor rights, on the grounds that the new environmental regulations restricted its business and diminished the value of its products. The dispute was heard by a NAFTA Chapter 11 arbitration panel, which had to determine whether such state intervention violated investment protection obligations. The arbitral tribunal dismissed Methanex's claims, finding that the United States' right to regulate environmental and public health matters (in this case, a ban on a toxic fuel additive) did not breach the country's international investment commitments. The tribunal emphasized that a state is entitled to take measures to protect public health and the environment, even if those measures adversely affect private investors. The decision noted that state sovereignty permits the implementation of regulatory measures for the protection of public interests (such as ecology and health), and that such measures do not violate international obligations as long as they are not a disguise for protectionism or a means of unlawful discrimination. The Methanex award confirms that the "right to regulate" doctrine can legitimize state actions taken in the public interest, even when they harm foreign companies' interests, provided those actions are enacted in good faith and do not contravene express commitments.

Legal scholars have further elaborated on these issues. Anthony Anghie observes that multinational corporations often wield significant leverage that can constrain states' ability to pursue independent policies. Therefore, the

RTR doctrine is important for maintaining legal equilibrium, as it grants states the ability to regulate corporate activities in the public interest [Anghie, 2023]. Jellinek, drawing on St. Augustine's vision of the "City of God" and the need to limit power, offered secular arguments to justify the state's monopoly on authority. In his conception of state personality, Jellinek argues that the power of the state is unique because the state binds itself to obey the legal order. The Holy See again serves as an illustrative example: despite lacking traditional attributes of statehood (such as territory and a permanent population), it plays a significant role on the international stage, acting with a form of spiritual sovereignty and actively defending human rights, engaging in humanitarian efforts, and spreading the values of international law [Лычковский, 2011].

Martti Koskenniemi and other jurists support the view that international law must adapt to new challenges of globalization while preserving the sovereign rights of states [Simpson, Koskenniemi, 2002]. The existence of RTR provides a legal basis that enables states to exercise their sovereign prerogatives while still ensuring the protection of foreign investors' interests. In this regard, the experience of unique actors like the Holy See is noteworthy: despite its unconventional legal status, it continues to participate actively in international affairs, upholding humanitarian and moral principles [Дьяченко, 2006].

As Maxim Likhachev notes, international legal personality is a dynamic concept that changes with historical context and social conditions. In his view, the evolution of personality in international law reflects growing inclusiveness and a desire for the law to account for the needs of human beings, not only state actors [Лихачев, 2023]. By contrast, Affolter observes that a state's legal personality is a dynamic process which develops gradually and cannot be permanently fixed. A state, acting as a legal person, must constantly reassess the boundaries of its authority in order to maintain a balance between legal norms and the practical exercise of power [Affolter, 1906]. In international law, this is evidenced by the development of stabilization clauses and umbrella clauses in international contracts, which help protect the interests of all parties and ensure predictability and stability in legal relations.

The “right to regulate” doctrine plays a central role in ICCL by enabling states to protect public interests through sovereign regulation of construction contracts and investment projects—evaluating their impact on citizens, the environment, and sustainable development and, where necessary, acting contrary to prior agreements. In doing so, a balance is maintained between the need to uphold legal stability for investors and the preservation of states’ sovereign rights. A key conclusion from this study is that parties to international construction contracts must account for the RTR doctrine when forming agreements. This is not merely a theoretical notion but a practical approach aimed at proper risk assessment and allocation, as well as realistic forecasting of how state and non-state actors might invoke RTR in influencing the execution of major construction and investment projects.

## **Regulatory Authority in International Construction Contracts: Managing Sovereign Risk, Investor Rights, and Cross-Border Dispute Resolution**

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*The chapter analyses the impact of the doctrine of the right to regulate on state and non-state legal personality within international construction contract law. It begins with Georg Jellinek’s concept of voluntary self-limitation and proceeds to the Holy See, the United Nations and the United States as examples of distinct personalities shaping regulatory clauses. Arbitral awards in SAUR International SA v. Argentina and Methanex v. United States delineate legitimate boundaries for public-interest intervention. The discussion concludes that embedding the right to regulate in construction contracts reallocates regulatory risk and enhances predictability and investor confidence in complex infrastructure projects.*

The review of arbitral practice, including SAUR International SA v. Argentina and Methanex v. USA, demonstrates the importance of anticipating potential

regulatory initiatives by states. Further inquiry is warranted into the application of the RTR doctrine in the activities of non-state actors, since their actions are governed both by international law and by sovereign domestic legal systems.

Overall, the RTR doctrine provides a robust legal foundation for state action, allowing governments to respond flexibly to the challenges of a multipolar world while preserving their sovereign rights. In the context of international construction contracts, this doctrine helps to achieve a balance between the rights of states and investors, which in turn contributes to a predictable and stable legal environment. Notably, the results of this research indicate that the International Federation of Consulting Engineers (FIDIC), which develops global standards in this area, should take the RTR doctrine into account in its model contracts and guidelines so that such considerations are reflected in the ICCL framework.

The approach proposed herein—to integrate the RTR doctrine into international construction contracts—constitutes a new method of allocating normative risks between the parties. This approach can aid in developing effective legal mechanisms that foster stability and predictability in the regulatory environment for international investments.

### **Note on the publication of the main research results**

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