Towards a Repository of Policy Options for IIA Reform

Research Project
Investor-State Dispute Settlement ('ISDS') and Alternatives of Dispute Resolution in International Investment Law[1][i]

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The study[ii] was prepared from April to September 2014, published on 22nd September 2014, and presented to the members of INTA and JURI Committees during a public hearing on 27th January 2015. The main findings are as follows:
The EU should include state-of-the art investment chapters in all of its comprehensive free trade agreements or, where appropriate, should negotiate stand-alone investment agreements. Substantive commitments should be backed up by an **investor-state dispute settlement mechanism**.

By including modern investment chapters in all EU free trade agreements, the EU would make an **important contribution to the development of the international rule of law** and, simultaneously, **protect European investments abroad**.

To the extent that the study considered CETA draft texts, overall it **welcomes the progress made by the European Union** in improving the current investment protection regime. If compared to many older investment agreements in force, including those of EU Member States, **CETA breaks new ground**. It displays a **new quality of investment treaty making in Europe**. Largely borrowing from Canadian and US American models, CETA defines substantive standards in more detail. Frequent reference is made to the right to regulate, and investment arbitration is made more transparent and, in tendency, may appear less biased.

While explicitly acknowledging progress made with the regulatory approach taken in CETA, **five significant challenges remain to be resolved**. Interestingly, three out of four issue areas are also identified as "areas for further work" in the Commission's Report on the Online public consultation on investment protection and investor-to-state dispute settlement (ISDS) in the Transatlantic Trade and Investment Partnership Agreement. Substantive provisions in EU investment agreements were not in the focus of the study.

The four issue areas relate to the following:

1. **The current CETA text** does not only **insufficiently incorporate national legal systems**; it **weakens functioning** judiciaries such as the **French, Dutch or European** ones. Strengthening the rule of law in the international sphere is exchanged against a weakening of the same at a national level.
2. **The current CETA text does not establish an appeals facility but only vaguely alludes to it**. **Legal errors and errors of fact or conflicting interpretations** of international arbitral tribunals formed under CETA **can hardly be corrected effectively**. Consistency in the interpretation and application of the Agreement cannot be guaranteed for.
3. **The current CETA text does not dispel** a possible public **perception of a tribunal's bias in favour of investors**. Arbitral proceedings against states can almost exclusively be initiated by investors in a meaningful manner. The ad hoc arbitrators and counsel – constantly changing their roles – will

[1] The opinions expressed in this paper are those of the author and do not necessarily reflect the views of the UNCTAD Secretariat or its Member States.

continue to see themselves subject to the accusation of furthering their business interests by an actual or perceived investor-friendly decision-making practice.

4. **The current CETA text leaves administrative issues potentially critical to procedural outcomes**, such as the selection of arbitrators, up to the ICSID Secretariat, part of an **international organization in which European forces are traditionally of no dominance**.

What Europe needs is an independent, innovative ISDS model, which protects investors and observes European and Member State interests.

A European ISDS model can **protect investments abroad** in a **sustainable** fashion, thereby setting **new global standards and providing stimuli for investment**, bringing government regulation and private ownership interests in a reasonable balance and contributing to conveying **Member State and European values and legal convictions**.

Such a European model

1. **sufficiently incorporates functioning national and European courts** in the settlement of disputes between investors and their host state. This may especially be realized by an **elastic local remedies rule** dependent on the independence and competence of the respective national legal system in a given case. The extent of this obligation to exhaust local remedies can be determined by a rule of law index and adjusted flexibly.
2. **creates a permanent appeals facility for investment disputes** that may not only be invoked in the context of arbitration on the basis of EU agreements but may also potentially be open to arbitration on the basis of agreements from third countries.
3. **mitigates the perception of bias** in favour of investors **in ad hoc arbitral tribunals. This can be achieved by a significant increase in the group of potential arbitrators** who shall be nominated for arbitration **based on their placement on a respective list**. Access to the list shall principally be open to each and every lawyer qualified for investor-state arbitration. In the long run ad hoc arbitration could be dismissed in favour of reviewing the exercise of governmental authority by a permanent court.
4. possibly **delegates administrative decisions** crucial to arbitral outcomes, such as the appointment of arbitrators, to an **international (arbitral) institution based in Europe**, which shall provide reasonable assurance as to its neutrality by virtue of its organization and status as an international organization. Alternatively, the ICSID Secretary-General should not enjoy discretion in its administrative decisions on the basis of CETA.

[i] The study, which was commissioned by and prepared for the European Parliament, INTA-Committee, Brussels, Belgium, 2014, is part of the "Studies on Investor-State Dispute Settlement provisions in the EU's international investment agreements (ISDS)" by Pieter Jan Kuijper, Study on Investment Protection Agreements as Instruments of International Economic Law, pp 8-38; Steffen Hindelang, Study on Investor-State Dispute Settlement ('ISDS') and Alternatives of Dispute Resolution in International Investment Law ('ISDS Study for the EP'), pp 39-131; Ingolf Pernice, Study on International Investment Protection Agreements and EU law, pp 132-169; all in: European Parliament, Directorate-General for External Policies, Policy Department, Investor-State Dispute Settlement (ISDS) Provisions in the EU's International Investment Agreements, Volume 2-Studies, Brussels 2014.

Annex:

A provision which sufficiently incorporates functioning national and European courts could read as follows:

Art. X.21 Procedural and Other Requirements for the Submission of a Claim to Arbitration

[(0)] *The Parties recognize the subsidiary nature of the arbitration mechanism established by this Chapter and the fundamental role which national authorities, i.e. governments, courts and parliaments, must play in guaranteeing and protecting rights accruing to an investor, irrespective of whether domestic or foreign, at the national level. In this respect, the Parties undertake to provide effective legal remedies in their domestic legal systems.*

[(1)] An investor may submit a claim to arbitration under Article X.22 (Submission of a Claim to Arbitration) only if the investor:

[…] [lit. (a) to (e) as in CETA]

[(f)] where it has initiated a claim or proceeding seeking compensation or damages before a tribunal or court under domestic or international law with respect to any measure alleged to constitute a breach referred to in its claim to arbitration, provides a declaration that:

[i.] a final award, judgment or decision has been made; or

[ii.] it has withdrawn any such claim or proceeding;

[(f)bis] where it has not initiated a claim or proceeding before a tribunal or court under domestic law with respect to any measure alleged to constitute a breach referred to in its claim to arbitration, provides a declaration that domestic remedies are unavailable or ineffective;

The declaration *in accordance with lit. [(f)] or [(f)bis]* shall contain, as applicable, proof that a final award, judgment or decision has been made or proof of the withdrawal of any such claim or proceeding, *or the circumstances substantiating that local remedies are unavailable or ineffective;* and

[(g)] waives its right to initiate any claim or proceeding seeking compensation or damages before a tribunal or court under domestic or international law with respect to any measure alleged to constitute a breach referred to in its claim to arbitration.

[…] [subparagraphs (2) to (3) as in CETA]

[(4)] Upon request of the respondent, the Tribunal shall decline jurisdiction where the investor […] fails to fulfil any of the requirements of paragraphs 1 and 2.

In case the investor provides a declaration under subparagraph [(1) lit. (f)bis], the tribunal shall, when establishing whether the investor has fulfilled the said requirements, take into account:

[(a.)] the overall degree of development of the domestic legal system in terms of the rule of law as evidenced in the most recent United Nations Rule of Law Indicators, EU Justice Scoreboard, the World Justice Project (WJP) Rule of Law Index, and the Bertelsmann Transformation Index [choice of indexes for illustrative purposes only];

[(b.)] the availability of a domestic remedy in the individual case, i.e. a domestic remedy must exist within the domestic legal system and can be pursued without difficulties or impediments by the investor;

[(c)] the effectiveness of a domestic remedy in the individual case, i.e. a local remedy must offer a reasonable prospect of success.

A domestic legal system shall be assumed making available effective domestic remedies when ranked among the top ten percent [choice of percentage for illustrative purposes only] on an average calculated from all Indexes referred to in subparagraph (4) (a), except in the rare circumstance where the investor can establish facts from which may be assumed that the investor was treated in a way which may amount to denial of justice.

[subparagraph (5) as in CETA]

A provision which would reduce the discretion in administrative decisions could be drafted as follows:

Article X.25: Constitution of the Tribunal

[subparagraphs (1) to (2) as in CETA]

[(3)] The Secretary-General of ICSID shall, upon request of a disputing party, appoint the remaining arbitrators from the list established pursuant to paragraph 4 *in the order established therein. An arbitrator from the list established pursuant to paragraph 4 can only be reappointed if the said list has been exhausted*. In the event that such list has not been established on the date a claim is submitted to arbitration, the Secretary-General of ICSID shall make the appointment at his or her discretion taking into consideration nominations made by either Party and, to the extent practicable, in consultation with the disputing parties. The Secretary-General of ICSID may not appoint as presiding arbitrator a national of either Canada or a Member State of the European Union unless all disputing parties agree otherwise.

[subsequent subparagraphs as in CETA]