

Towards a Repository of Policy Options for IIA Reform

Meeting

ISDS - what is it and the arguments for and against including such a provision in a Transatlantic trade and investment deal¹

All-Party Parliamentary Group on EU-US Trade & Investment Meeting on TTIP and ISDS, 4 November 2014, London, United Kingdom

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The meeting was attended by Parliamentarians from opposition and government Parties, plus representatives from business, trade unions and campaign organisations and interested individuals. Below is a short summary of the remarks and discussion.

Dr Zhan provided the big picture on investment agreements. There is no multilateral investment regime. Instead there are more than 3,200 bilateral or regional agreements, the majority of which include provisions on how to deal with disputes (ISDS). These agreements provide a kind of “insurance policy” against certain political risks. ISDS provisions have not been widely used (568 cases by end 2013). Most claims have been raised by companies from the EU and the US against governmental practices in developing countries. In recent years there has also been an increase in cases raised by companies from EU states against other EU states. In total, EU companies have initiated 300 cases while US companies have filed 127 disputes since 1987s.

UNCTAD has summarized the concerns about ISDS as relating to, legitimacy, transparency, “nationality planning” by investors, lack of appeal mechanism, inconsistency of arbitral decisions, arbitrators’ independence and impartiality and financial stakes involved. UNCTAD has also identified potential paths for reforming the ISDS system, which include:

- Promoting alternative dispute resolution,
- Modifying the existing ISDS mechanism through individual IIAs,
- Limiting investors’ access to ISDS,
- Introducing an appeals facility,
- Creating a standing international investment court.

Dr Zhan underlined that ISDS is only part of the problem, and not the root of the problem, given that ISDS tribunals merely *apply* the law (treaty). He called for a comprehensive reform effort of both investment agreements and investment dispute mechanisms.

Dr Poulsen argued that a convincing, concrete and evidence-based case for the inclusion of ISDS in a Transatlantic trade and investment treaty had yet to be made. He underlined that the investor-state arbitration mechanism had been developed in order to safeguard investors in countries with poor judicial systems, and there is therefore no need for such a mechanism between most EU countries and the US. He further questioned whether ISDS in TTIP would act as an effective precedent for countries like China, India, and Brazil, and warned that public concerns raised about ISDS were removing attention from more important elements under negotiation in the agreement. If substantive investment protections should be included into TTIP he suggested following the Australia-US FTA, where the investment chapter is backed up by state-to-state dispute settlement only.

Dr Calamita also described the background for including ISDS as a concern with the rule of law in a

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.

country. Investment Agreements regularly provide protection against discrimination, expropriation, unfair and non-equitable treatment and restrictions on transfer of capital. ISDS is a means of resolving disputes about breaches of such protection. The motivation for including ISDS in the North Atlantic Free Trade Area (NAFTA) was the legal conditions in Mexico; the inclusion in the Energy Charter Treaty was based on the legal conditions in Russia. Once an ISDS mechanism is in place, however, it will be attempted used, Canadian firms had raised cases against the US and vice-versa. ISDS would provide firms with greater compensation than that which is provided for under UK law, but States could also choose to limit compensation in an agreement. An investment agreement where the EU, the US and Canada agree on the same principles and dispute provisions could set a “gold standard” for other countries as the three together account for 55% of global foreign direct investments (FDIs).

In the ensuing discussion it was pointed out that it is not ISDS that determines whether public services or government procurements are subject to litigation, but the investment commitments themselves. Governments determine which policy areas will be subject to commitments and are free to “carve out” areas. Poulsen argued for agreeing on basic principles instead of carving out areas as areas on an ad-hoc basis as salient policy concerns change over time.

Small and medium sized enterprises will be unlikely users of ISDS both because of the costs involved in cases (average minimum of \$4 million) and a lack of legal expertise. Only through associations or a pooling of resources could SMEs reasonably utilize ISDS.

Some of the rhetoric around ISDS was termed “overblown”. The European Commission has attempted to clarify investment commitments improve the regulatory space and improve dispute settlement provisions. Particularly the efforts to increase transparency were highlighted by Dr Zhan. Without ISDS in a transatlantic context existing bilateral treaties could still be used as vehicles for pursuing dispute cases.

It was questioned whether investment agreements and ISDS are important to promote foreign investment flows. Dr Zhan focused on factors, such as the policy environment, the economy and infrastructure of a country as being more determinative for investment flows.

While the US and UK may provide similar levels of investor protection the legal system in some member states in the EU may not provide the same protection. The existence of bilateral treaties between many EU member states and the US and the “new” EU member states provide a disparate regime. The question was raised if the introduction of ISDS in a Transatlantic treaty could be differentiated between EU member states. While possible, such differentiation could result in systemic dilemmas with regard to equal treatment.

ISDS was compared to an insurance policy or a seat-belt in a car. The seat belt does not determine where the car drives or how fast or efficiently, but is there to protect in case something goes wrong. The key question going forward is whether such a system is justified in a Transatlantic agreement, and if so; on what terms.

ⁱ The All-Party Parliamentary Group on EU-US Trade & Investment organized an informative and authoritative assessment of investor-state dispute settlement (ISDS) provisions in the context of TTIP on November the 4th in Portcullis House with the following panelists: Dr James X. Zhan, Director of Investment and Enterprise Division, UNCTAD; Dr Lauge Poulsen, Assistant Professor in International Political Economy at University College London; Dr N. Jansen Calamita, Director of the Investment Treaty Forum at the British Institute of International and Comparative Law.