EXASPERATION IN INVESTMENT TREATY ARBITRATION

European Branch

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EXASPERATION

With regulatory competence in Europe

- Competence in Article 207 of the Treaty on the Functioning of the European Union («TFEU», 2008) and Article 5 Lisbon Treaty (2009)

With investor-state dispute resolution worldwide

- EU: difficulties in TTIP negociations
- Bolivia (2007), Ecuador (2009), Venezuela (2012), opted out of ICSID
- Australia (2011): no more investor-state dispute resolution mechanism in trade agreements

EU REGULATORY COMPETENCE

- **Article 207 TFEU**

1. The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union's external action.

- **Article 5 (2) Lisbon Treaty**

2. Under the principle of conferral, the Union shall act only within the limits of the competences conferred upon it by the Member States in the Treaties to attain the objectives set out therein. Competences not conferred upon the Union in the Treaties remain with the Member States.

EU REGULATORY COMPETENCE

- Distinction between Intra- and Extra-EU BITs:
  - Extra-EU BITs:
    - Prior to entry into force of Lisbon Treaty: parallel competences EU/ Member States
    - Lisbon Treaty: «conferred upon»
    - For some time, no transitional provision
    - 2012: Regulation No. 1219/2012 establishing transitional arrangements for bilateral investment agreements between Member States and Third Countries
      - All BITs entered into by Member States prior to the entry info force of the Lisbon Treaty are maintained into force until they are replaced by an EU investment agreement
      - For BITs entered into after Lisbon Treaty, Member States are authorized to enter into negociations to bring them in compliance with EU law
      - Member States may negotiate new BITs as long as conditions set forth by Commission are met

EU REGULATORY COMPETENCE

- Intra-EU BITs:
  - Commission fears discrimination between Member States
  - Result: all Intra-EU BITs must be terminated or left unapplied
  - Legal uncertainty:
    - Reliance on EU law may reduce investment protections
    - Member States may question jurisdiction of arbitral tribunals in favor of ECJ
    - Member States may argue that accession to EU terminated BIT

EU REGULATORY COMPETENCE

- Intra-EU BITs – case law
  - *Eastern Sugar v Czech Republic (2007)*: No automatic termination of BITs when accession into the EU, despite position of the Commission that BIT automatically superseded by EU law.
  - *AES v Hungary (2010)*: claim by investor under the ECT following Hungary's termination of power purchase agreements («ppa») upon concerns by Commission that ppa violated EU regulations on prohibition of state aid.
    - Tribunal: no decision on whether EU law takes precedence over ECT but Hungary's decision a rational public measure

EU REGULATORY COMPTENCE

- *Eureko v. Slovak Republic (2010):*
  - *Award:* jurisdiction under the BIT extends to the application of EU law, both as a matter of international law as a matter of German law
  - *Frankfurt court (annulment proceedings):* Claim for annulment rejected
  - *German Supreme Court*: Proceedings redundant because final award in favor of investor in the meantime. Supreme Court decided to await Slovakia's appeal of the award on the merits.
    - Matter might end up before ECJ since German Supreme Court is arguably obliged to refer the matter toECJ

BACKLASH AGAINST ISDS

- In the EU
  - Transatlantic Trade and Investment Partnership (TTIP):
    - US – EU
    - Negociations started in June 2013
    - Suspension negociations over ISDS clause to allow for consultations of European Public
      - Germany has insisted that TTIP must exclude investor-state dispute settlement
        - Ground: US investors have sufficient protection in the EU courts

BACKLASH AGAINST ISDS

- WORLDWIDE:
  - *Bolivia*: denunciation of ICSID in 2007 as a gesture of protest against numerous arbitrations that followed Bolivia's nationalization of the hydrocarbon industry
  - *Ecuador*: Investors claims following change in hydrocarbons law. Denunciation of ICSID in 2009
  - *Venezuela*: Nationalization of Cerro Negro oil project and other industries by Chavez. Claims by investors. Withdrawal from ICSID in 2012.
  - *Australia*: rejection of ISDS in all trade agreements in particular in Trans-Pacific Partnership.

BACKLASH AGAINST ISDS

- Expressed reasons for backlash:
  - Lack of trust in ISDS following «extreme» cases:
    - *Vattenfall v Germany*: Swedish company Vattenfall is currently seeking compensation from Germany for its decision to phase out nuclear power following the Fukushima disaster
    - *PMI v Australia*: Philip Morris is seeking compensation from Australia for lost income following the introduction of plain packaging laws for tobacco products

SOLUTION?

- Commission's Factsheets (October/November 2013): Position of EU Commission on investor-state dispute settlement.
- Rebalancing the system- a two-pronged approach:
  - Clarifying and improving investment protection rules:
    - Investor-state dispute resolution mechanisms does not limit the EU's right to regulate FDI
    - Guidance for arbitrators on indirect expropriation
    - Setting out precisely «fair and equitable treatment»
  - Improving how the dispute settlement system operates:
    - Loser pays all rule
    - Publicity of all submissions and awards
    - Code of conduct for arbitrators
    - States can maintain control over how investment provisions are interpreted

SOLUTION?

- Application of these principles in CETA (2013)
  - «Comprehensive Economic and Trade Agreement» with Canada
    - Right to regulate to pursue legitimate public policy objectives such as the protection of health, safety, or the environment;
    - Precise definition of Fair and Equitable treatment:
      - Denial of justice in criminal, civil or administrative proceedings
      - Fundamental breach of due process, including a fundamental breach of transparency, in judicial and administrative proceedings
      - Manifest arbitrariness
      - Targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief
      - Abusive treatment of investors, such as coercion, duress and harassment. In addition, a breach of legitimate expectations is limited to situations where the investment took place only because of a promise made by the State that was subsequently not honoured

SOLUTION?

- Indirect expropriation: substantial deprivation of the attributes of property
- Full protection and security does not cover protection against changes of laws and regulations
- Investment: only assets that possess the characteristics of investment: commitment of capital or other resources, expectation of gain or profit, assumption of risk, certain duration
- Investor must have substantive business operations
- Investor-state dispute settlement system:
  - Prohibitions on seeking remedies in domestic courts and through investor-state dispute resolution at the same time, whilst encouraging the use of domestic court
  - Increased certainty for states through the setting of time periods after which a claim cannot be made (in principle 3 years)
  - Increased consistency and strengthened protection against possible conflicts of arbitrators through the need for agreement on the arbitrators, failing which the arbitrator will be chosen from a roster of arbitrators, jointly decided by the European Union and Canada

SOLUTION?

- Introduction of a binding Code of Conduct for arbitrators;
- Strong protections allowing for frivolous claims to be rejected very quickly where the case is manifestly unfounded and where the tribunal, even if facts are assumed to be correct, cannot rule in favor of the investor
- Strong protection against unfounded claims
- Full transparency – all documents public, all hearings open, submissions by interested parties
- Possible appellate mechanism
- Encouragement of alternative dispute resolution – explicit provisions for mediation for investment disputes
- Absolute clarity that a state cannot be forced to repeal a measure
- Effective mechanisms for the Parties to the agreement to issue binding interpretations on what they originally meant in the agreement and to take part in arbitrations on questions of interpretation
- Action against spiralling costs through effective limits to the costs of the arbitration
- Investor-state dispute resolution only applies to alleged breaches of the investment protection standards and does not apply to market access

PARTING WORDS

- Investor-State Dispute Resolution:
  - Not the best, but generally better than the alternative (domestic courts)
  - Possibility to go before domestic courts remains in most Treaties (fork-in-the-road or preliminary proceedings)
  - Learned from mistakes: new language helps curing abuse
  - For States:
    - Investment protection improves investment climate
    - Negociation tool
  - For Investors
    - Investment arbitration may constitute only protection for small investors
    - Protection against dependence on the host State's actions

THANK YOU!

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