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Manuscript

Presentation of Studies on

Investor-State Dispute Settlement provisions in the EU's international investment agreements (ISDS)

European Parliament JURI/INTA Joint Public Hearing on the Transatlantic Trade and Investment Partnership (TTIP): Regulatory Aspects and Investor-State Dispute Settlement/Arbitration on 27.01.2015

Mr. Chairman, Members of Parliament, ladies and gentlemen,

Thank you very much for the opportunity to present briefly the main findings of three studies on investor-State dispute settlement ('ISDS') provisions in EU investment agreements, commissioned by the INTA Committee and published late last year.

The authors – Professor Kuijper, Professor Pernice, and I – very much hope to contribute with these works towards objectifying the current debate on investment protection in CETA, TTIP, Singapore, and other agreements currently under discussion.

Let me start right away with what I perceive as the most important message all three studies broadly have in common: **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 by an **investor-State dispute settlement mechanism**.[i]

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 studies have already considered CETA draft texts[ii], overall they **welcome 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, less partial.

While explicitly acknowledging progress made with the regulatory approach taken in CETA, **five significant challenges remain to be resolved**.

Interestingly, four out of five 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.[iii] Substantive provisions in EU investment agreements were not in the focus of the three studies I present here.

The five 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, to some extent, exchanged against a weakening of the same at a national level.[iv]

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.[v]

3. **The current CETA text does not sufficiently 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 continue to see themselves subject to the accusation of furthering their business interests by an actual or perceived investor-friendly decision-making practice.[vi]

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**.[vii]

5. **The dispute settlement mechanism contained in the CETA text might not fully be compatible with the EU Treaties** as it does not pay sufficient regard to the Court of Justice of the European Union's judicial monopoly and the principle of autonomy of EU law.[viii]

What Europe needs instead 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, furthering the respect of human rights, 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 be 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 the tribunal on the basis of a rule of law index and adjusted flexibly.[ix]

2. **creates a permanent appeals facility for investment disputes** that may not only be invoked in the context of arbitration on the basis of a specific EU agreement but may also potentially be open to arbitration on the basis of agreements from third countries.[x]

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 to sit in an 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.[xi] In the long run ad hoc arbitration could be dismissed in favour of reviewing the exercise of governmental authority by a permanent court.[xii]

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. [xiii] Alternatively, the ICSID Secretary-General should not enjoy any discretion in its administrative decisions on the basis of CETA and any other EU agreement.[xiv]

5. **A European Model must sufficiently safeguard the autonomy of EU law and the CJEU's judicial monopoly.** This is only to be achieved if the EU legal order is shielded from spillover effects flowing from investment arbitration. When questions of EU law arise in arbitration, even if only indirectly, the CJEU might have to be involved by providing binding interpretations.[xv] In order to avoid any uncertainty, a draft ISDS text in an EU agreement should be submitted to the CJEU for a legal opinion before it is concluded and ratified.

All in all, the European Commission has been successful in submitting an updated investment chapter in CETA arriving largely at North American standards. If compared to other agreements, in particular to such of the Member States, improvements are visible. However, significant drawbacks remain. Since no agreement has been concluded yet, this is the opportunity for Europe and its Parliament to put forward solutions that would make European investment protection fit, attractive, and sustainable for the years to come.

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[i] 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.

[ii] For the purpose of these speaking notes CETA Text dated 26.9.2014 has been used.

[iii] European Commission, SWD(2015) 3 final.

[iv] Hindelang, ISDS Study for the EP, pp 76-78, pp 83-93.

[v] Ibid. pp 64-66, p 108.

[vi] Ibid. pp 100-104.

[vii] Ibid. pp 100-101.

[viii] Pernice, Study on International Investment Agreements and EU Law for the EP, pp 145-151.

[ix] Hindelang, ISDS Study for the EP. pp 76-78, especially pp 83-93. 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]

[x] Ibid., pp 64-66, S. 108. The issue of arbitration costs must, of course, be addressed, especially with regard to small and medium-sized enterprises. Alternatively one could also consider a preliminary ruling procedure for the binding interpretation of an agreement by the contracting parties.

[xi] Ibid., pp 100-104.

[xii] Ibid., pp 61-63.

[xiii] Ibid., pp 100-101; in addition, a European Model guarantees *fair, transparent* (see ibid., pp 98-100) *and independent ISDS proceedings*, the *access of the public* to said proceedings (ibid., pp 98-100), *control over the agreement through the EU and its contracting partners*, especially *by means of the binding interpretation* of agreement clauses by its signatories (ibid., pp 66-70, 83-85) and permits the die *regular review and, if necessary, amendment of the ISDS clauses* in the agreement through the State parties (ibid., p 96).

[xiv] 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]

[xv] Pernice, Study on International Investment Agreements and EU Law for the EP, pp 151-160. The *constitutional limits of transferring jurisdictional authority to arbitral tribunals* in the area of public law disputes are, furthermore, to be observed.

Check against delivery.

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Key findings I

- 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**
- Progress made by the European Union in improving the current investment protection regime - **CETA breaks new ground**

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Key findings II

Five significant challenges remain to be resolved in respect of the CETA model as it

1. **insufficiently incorporates national legal systems,**
2. **does not establish an appeals facility but only vaguely alludes to it,**
3. **does not sufficiently dispel a possible public perception of a tribunal's bias in favour of investors,**
4. **leaves administrative issues potentially critical to procedural outcomes to an international organization in which European forces are traditionally of no dominance, and**
5. **the dispute settlement mechanism in the CETA model might not fully be compatible with the EU Treaties**

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Key findings III

- **Europe needs an independent, innovative ISDS model, which protects investors and observes European and Member State interests**
- **A European model**
  1. sufficiently **incorporates functioning national and European courts** in the settlement of disputes between investors and their host State **by means of an elastic local remedies rule**
  2. **creates a permanent appeals facility** for investment disputes, also **open to third country agreements**

Key findings IV

- **A European model (continued)**
  3. **mitigates the perception of bias** in favour of investors **in ad hoc arbitral tribunals by a significant increase in the group of potential arbitrators who shall be nominated to sit in an arbitration based on their placement on a respective list,**
  4. **delegates administrative decisions** crucial to arbitral outcomes, such as the appointment of arbitrators, to an **international (arbitral) institution based in Europe**,
  5. **must sufficiently safeguard the autonomy of EU law and the CJEU's judicial monopoly.**

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Thank you for your attention!

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