



The 3d Vienna Investment Arbitration Debate

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The European Union's approach to investment dispute settlement.

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It is an honour to be here today at 'The 3d Vienna Investment Arbitration Debate' and to be asked to deliver these remarks.

I welcome the chance to be here in front of such a distinguished audience and to try to set out the EU's views on reform of investor state dispute settlement.

We live in an era of unparalleled scrutiny. The internet, in particular, has opened up the realm of public debate far beyond what previous generations could have ever imagined.

That vigorous public debate now also shapes the polities in which we operate. It

behoves us therefore to continuously critically examine the choices previous generations have made and to seek to adapt them or reform them where necessary.

That vigorous public debate has in recent years focussed part of its energy on investment protection and investor state dispute settlement. To those of us who have been active in or following this field over the years it can come as little surprise that this debate arises. Ultimately, we need to accept and embrace this public debate. Any public policy needs to be responsive to the polities which validate it.

Set against this vigorous public debate, I would like to focus in my remarks on four groups of issues.

- First, I'd like to address some of the conceptual issues that surround the debate on ISDS;
- Second, I'd like to discuss the EU's opinion on this debate;
- Third, I'd like to sketch out the main ideas for the establishment of a Multilateral Investment Court; and
- Fourth, and finally, I'd like to address the process, with a particular focus on the UNCITRAL discussions.

In looking at these issues, I would like to leave you with two key messages. The first is that the reform process is a serious endeavour. The EU is far from being alone in seeing the need for reform of ISDS. Many other countries are engaging in that process. The second is that we have learnt a lot over these last years both in the investment field and

in other fields. It is vital that that knowledge and expertise be brought to bear in ISDS reform discussions.

1. Conceptual issues around ISDS

Let me first address some of the conceptual issues which arise around ISDS.

Much of the criticism of the investment protection and ISDS system comes from the concern that it is a system which impacts and limits genuine regulatory activities.¹ One could consider this surprising. After all, the key substantive investment protection obligations are commonplace in other legal systems and are not considered inimical to the ability of states to regulate.

In particular, most favoured nation and national treatment obligations can historically be found in many treaties, most notably in the GATT/WTO system. There is surely in principle nothing objectionable in an obligation not to discriminate. In particular, an obligation not to discriminate says nothing about the ability of a state to regulate, simply that it must not do so in a discriminatory manner.

¹ See Pollack, Mark A., *The New, New Sovereignism (Or, How the Europe Union Became Disenchanted with International Law and Defiantly Protective of Its Domestic Legal Order)* (April 21, 2017). Chiara Giorgetti and Guglielmo Verdirame, eds., *Concepts on International Law in Europe and the United States* (Cambridge University Press, Forthcoming). Available at SSRN: <https://ssrn.com/abstract=2956738> or <http://dx.doi.org/10.2139/ssrn.2956738>

Similarly, protection against uncompensated expropriation is commonplace in many legal systems. It forms part of the European Convention on Human Rights and is found in many national constitutions, particularly in Europe. But Europe has also legislated to achieve a very high standard of regulation for the protection of the environment or labour rights. So it cannot be the case, per se, that protection against uncompensated expropriation is by definition contrary to the right to regulate.

A similar case can be made concerning the fair and equitable treatment standard. If this is considered as comparable, in general terms, to protections offered under administrative law or systems of judicial review, there is nothing that stands in the way of the development of sophisticated regulatory practices. There is no reason, and indeed it would be a matter of concern, for regulatory activities to be carried out in a manifestly arbitrary way, to take but one example.

So if there is no substantive problem as such, where does the problem lie? Is it that foreigners are granted rights to defend their interests? Clearly, in certain quarters, that is an issue. But it behoves us, particularly now, to uphold international law. And international law is ultimately all about the reciprocal protection of the foreign interest. It's about imposing and accepting certain limits on a reciprocal basis so that actions of sovereign states do not have negative effects on foreign interests. That is, for example, the very foundational concept of the European Union. Accepting that this is the problem with investment protection and ISDS means negating the very core of international law. That clearly is a path we should not go down, in particular when we

know that so much of our economic growth depends on our ability to export and to invest in third country markets.

So where, then, does the issue arise? I want to suggest that it arises in the context of the dispute settlement mechanism for investment protection. It arises there because the ad hoc nature of a system, coupled with the public law nature of the disputes under treaties concluded between sovereigns is such that it fundamentally cannot provide the certainty and predictability about the core aspects of these investment protection standards that is required by all stakeholders, whether they be investors or governments or other interested parties. It is very difficult to point to a key decision taken by a tribunal and be able to honestly say that one knows that that particular decision will, with a high degree of certainty, be followed.

Compare and contrast this situation with that of the WTO Appellate Body. In the 1980s and 1990s there was much criticism of the GATT/WTO on the grounds that it privileged free trade interests over the ability of its Members to regulate, for example on environmental or health grounds. Similarly as for investment protection, one could argue that there is nothing inherent in the GATT rules which prevented a state from regulating, provided, for example, it didn't do so in a discriminatory manner. But the nature of GATT dispute settlement was such that one couldn't be confident that a decision by one panel would be followed by others. The change, and the key change I would argue, came with permanency. Permanency created by the establishment of the WTO Appellate Body. Since the Appellate Body is a standing body, in distinction to the *ad hoc* GATT and even WTO panels, one could have confidence that it's

pronouncements on, say the GATT Article XX exceptions, would be followed both by future panels and in later cases dealt with by the Appellate Body.

That stability and predictability which comes via permanency is absent from the ISDS regime. Whether we like it or not, it is indisputable that any tribunal may develop its own interpretation of a particular treaty norm. I am not arguing that there is not de facto a significant degree of following of precedent. However, there is nothing in the system, no permanency, which creates expectations in stakeholders that a particular approach will prevail.

And that, I would suggest, is the core question facing us today. That question is whether a system of dispute resolution with the key attributes of commercial arbitration remains the optimal system of dispute resolution for resolving investment disputes.

From an historical perspective, it is interesting to notice that when the ICSID Convention was drafted between 1961 and 1965, the model of commercial-style arbitration was transplanted to the system for the settlement of investor-State disputes, without differentiating between contract-based and treaty-based disputes, because the main types of disputes the ICSID drafters had in mind were disputes that the parties specifically agreed both *ex post* to submit to arbitration in a contract.²

² As JC Thomas and HK Dhillon note, the authors of ICSID considered that around 95 percent of cases would be under investment contracts and concessions and not under investment treaties, *see* JC Thomas and HK Dhillon, 'The Foundations of Investment Treaty Arbitration: The ICSID Convention, Investment Treaties and the Review of Arbitration Awards' (2017) 32(3) ICSID Rev-FILJ 459.

In the 1960's no one could predict the boom of investment treaty disputes. Today, however, investment disputes are predominantly based on treaties instead of contracts: up to 31 January 2018, only 25.2 percent of ICSID cases are in fact based on investment contracts or the investment law of the host state.³

This must lead us to rethink today if the initial choice of commercial-style arbitration for investment disputes was well made. If we had to make that decision again today, we would probably get to a different conclusion.

These questions are not purely European questions. The legitimacy crisis of ISDS has become a global issue. As discussions in UNCITRAL have shown, practically all states are wrestling with these questions.⁴ Policy makers and the investment community at large must take account of this and engage in the necessary reform of the ISDS system if they want the ISDS system to continue to apply in the future.

2. The EU's approach

The EU's policy approach first and foremost takes its cue from what investors and states alike need at the end of the process, i.e. access to a neutral, effective, legally predictable and coherent investment dispute settlement system.

³ See ICSID, 'The ICSID Caseload-Statistics' (Issue 2018-1) [https://icsid.worldbank.org/en/Documents/resources/ICSID%20Web%20Stats%202018-1\(English\).pdf](https://icsid.worldbank.org/en/Documents/resources/ICSID%20Web%20Stats%202018-1(English).pdf).

⁴ See the blog series by Anthea Roberts and Zeineb Bouraoui (<https://www.ejiltalk.org/uncitral-and-isds-reforms-what-are-states-concerns/>) analysing the concerns states have raised in the first two meetings of the UNCITRAL Working Group III posted on 5th and 6th June 2018.

Why should we maintain such a system? Indeed, the question has arisen as to whether investment protection and ISDS agreements actually create growth. It is difficult to argue that such agreements, in and of themselves, create such growth. The evidence is unclear, the debate unsettled. But the question, in any event, is more complicated than that because investors, and in turn policymakers, need to assess the utility of investment treaties and ISDS as part of a broader whole. No investor will invest just because of the existence of a BIT. Investors are primarily seeking the possibility to profit. But having a BIT or FTA with investment protection at one's disposal is clearly part of what an investor will take into consideration when weighing whether and at what price to make an investment. Consider the EU. One can say that investment protection rules exist in the EU treaties, through freedom of establishment and free movement of capital. These are backed-up by the possibility to remove the dispute, if necessary, from national jurisdictions, through, in particular, preliminary references to the Court of Justice. The point I want to make is that no-one isolates these rules to work out whether those treaty rules have an impact on investment, rather it is understood that the bundle of rights provided by the EU treaties, including those rights approximating the substantive standards of investment protection, create stability in which economic growth can take place.

We would make the case that investment protection and an effective and neutral dispute settlement system is key in creating a stable environment for companies to do business. It is one part of a bigger set of policies designed to foster growth through encouraging the creation of regional and global value chains which can spur growth, just as the EU

Treaty rules have done so within the EU. And it also has a rule of law component.⁵ The system of dispute settlement ensures that the law as contained in these international agreements can be enforced. It is to state the obvious that not all national legal systems incorporate international law and that no domestic courts, never mind how sophisticated they might be, are free from potential bias in the application of international rules even if they are incorporated into domestic law. We need to recall that one of the primary functions of the system of preliminary references within the EU is precisely to delocalise a dispute, to take it out of its national context, to ensure that the international nature of the obligation is not lost in the interpretation applied by the domestic courts. In that sense, investment dispute settlement is no different.

So how do we ensure that the system can be maintained in the medium term? How do we put it onto a sustainable footing? The answer, in our view, and as already foreshadowed, is in creating permanent bodies to settle these disputes. That, it is submitted, is the only way to ultimately respond to the concerns about the balance in these agreements and to address the concerns about the functioning of the current dispute settlement system.

In so doing we appeal to basic political norms that have governed our societies for the last centuries. “[It] is of fundamental importance that justice should not only be done, but should manifestly and undoubtedly be seen to be done” famously opined Lord Chief

⁵ Puig, Sergio and Shaffer, Gregory, *Imperfect Alternatives: Institutional Choice and the Reform of Investment Law* (June 14, 2018). *American Journal of International Law*, (2018 Forthcoming); Arizona Legal Studies Discussion Paper No. 18-22; UC Irvine School of Law Research Paper No. 2018-50. Available at SSRN: <https://ssrn.com/abstract=3191639>

Justice Hewart, building on the writings of Jeremy Bentham, Voltaire and Alexander Hamilton.⁶ Just as it would strike us and the man on the street as strange that permitting the disputing parties to appoint judges in a constitutional case before, for example, the Austrian Constitutional Court or the Austrian Supreme Administrative Court, so it should strike us as strange that in a treaty based case dealing with similar issues it should be possible for the disputing parties to appoint adjudicators. It certainly strikes the ordinary member of the public as strange.

And that takes me to the third part of my remarks. How should such a permanent body, and particularly a multilateral body, be structured.

3. The Multilateral Investment Court initiative

Let me first emphasise that the EU has purposely sought to build an inclusive, transparent and open process to discuss and develop responses to the issue of ISDS reform. We have of course our preliminary ideas on how this should be designed. The main features we would envisage would be as follows:

- The court would be permanent and be composed of a Tribunal of First Instance and an Appeal body;

⁶ R v Sussex Justices, Ex parte McCarthy ([1924] 1 KB 256, [1923] All ER Rep 233. See also Gaukrodger, D. (2017), "Adjudicator Compensation Systems and Investor-State Dispute Settlement", *OECD Working Papers on International Investment*, No. 2017/05, OECD Publishing, Paris, <https://doi.org/10.1787/c2890bd5-en>.

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- Consideration should be given as to how alternative dispute resolution can be enhanced in investment disputes, with a view to avoiding that disputes actually lead to litigation;
 - Appeal should not imply that a case is heard again *de novo*. An appeal should only be on issues of law and, we would suggest, on allegations that there has been a manifest error in the appreciation of the facts;
 - Both levels would be staffed by tenured adjudicators, working full-time on non-renewable terms;
 - The adjudicators should have expertise in public international law, ideally also knowledge of investment and trade. It will be important to ensure geographical representation and that gender balance is respected;
 - The adjudicators must be appointed by an effective mechanism to ensure high quality and competent adjudicators. Insights should be drawn from the practices of existing courts;
 - The court would only adjudicate claims brought under investment treaties that countries have expressly decided to assign to the authority of the court via a Mauritius Convention or BEPS type opt-in approach;
 - Enforcement would be ensured in a manner comparable with the current system
 - The court would have a secretariat to support its daily work;
 - Costs would be borne by the contracting parties, according to their ability to pay, meaning developing and least developed countries would pay less.

Consideration could be given to having users make some contributions, but clearly these should not be linked to the remuneration of the adjudicators ;

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- The procedures of the court should ensure transparency, we would suggest based on the UNCITRAL Rules on Transparency for ISDS;
 - It seems desirable to explore the creation of an Advisory Centre for developing countries; and,
 - special provisions to ensure access of SMEs to the court should be envisaged.

We are conscious that the move to state-appointed adjudicators is viewed with concern with the argument being made that the voice of investors will be lost in the appointment of adjudicators, to their detriment. However, that assumes a particular understanding of the paradigm in which these choices are currently made.⁷ Obviously, when a state is acting in the current system it will only act as a respondent, so it is entirely focussed on how its choice of arbitrator may assist it in its defence. That paradigm changes radically when a state is appointing permanent judges for future situations in which the state will not act exclusively as a respondent but will also have an interest that its investors' interests in a 3rd country be upheld. In that paradigm it will make very different choices from the scenario where it is already implementing its defence strategy.⁸

Let me also say that the EU takes the question of the best procedures for appointment extremely seriously. It is clear to us that the robustness of the process for appointment of judges will be a key point, if not the key point, in this project. On this issue we are

⁷ Roberts, Anthea, Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System (January 1, 2013). 107 American Journal of International Law 45 (2013). Available at SSRN: <https://ssrn.com/abstract=2033167>

⁸ See Roberts, Anthea, <https://www.ejiltalk.org/would-a-multilateral-investment-court-be-biased-shifting-to-a-treaty-party-framework-of-analysis/> published 28 April 2017. See also Puig and Shaffer, op cit. footnote 223.

fortunate. The last 80 or so years have seen the creation of many international courts and their appointment processes have been tried and tested. The international community has, we think, a good view of what works well and what doesn't work. Many scholars have been working on the functioning of international courts and the effectiveness of their procedures. So there is a wealth of real-life examples, experiences and academic analysis to build on. What will be important is that we have procedures for ensuring high quality candidates, that nominations be screened to ensure only the best candidates go forward and that an effective procedure focussing on an individual's abilities and competences be put in place. Rest assured that this will be a key focus for the EU in future discussions.

In any case, the EU is convinced that, in order to be a truly multilateral project, its design has to result from discussions with third countries and open and inclusive negotiations. This makes sense, because a multilateral solution will be optimal. As Shan Wenhua, a Chinese scholar, recently put it, we already have a spaghetti bowl of more than 3,000 treaties. If each country engages in its own piece-meal reforms, we will end up with a bowl-full of multiple strands of cut spaghetti (I think the Italians would call it "spaghetti spezzati", and safe to say it probably does not qualify as a highlight of Italian gastronomy!). Avoiding a bowl of spaghetti spezzati is clearly in everyone's interests, both investors and states. So it is important that work takes place at multilateral level on these issues.

4. The UNCITRAL process

That takes us to the UNCITRAL process. The United Nations Commission on International Trade Law (UNCITRAL) decided to initiate work on the multilateral reform of investment dispute resolution in July 2017.

For its discussions, UNCITRAL Working Group III has a broad three-step mandate to:

1. identify and consider concerns regarding ISDS;
2. consider whether reform is desirable in light of any identified concerns; and
3. if the Working Group concludes that reform is desirable, develop any relevant solutions to be recommended to the UNCITRAL Commission.

The first two rounds of discussions of Working Group III took place in Vienna (Austria) from 27 November to 1 December 2017 and in New York (US) from 23 to 27 April 2018. After its second meeting, the Working Group has finalised discussions on step 1 as regards a good number of concerns of ISDS and will proceed to consider whether reform is necessary as of its next meeting (in autumn 2018). This is without prejudice to additional concerns that may continue to be identified and considered. In late June 2018, the Working Group will report back to the UNCITRAL Commission on the progress achieved.

The EU strongly supports the UNCITRAL process given, among others, UNCITRAL's commitment to transparency, inclusiveness and accessibility: meeting reports and audio recordings of all Working Group sessions are published on the UNCITRAL website and participation is open to all UN members and to interested parties. International organisations are fully involved and can bring their expertise to bear. We benefit in

particular from the presence of the OECD, UNCTAD, ICSID and the PCA. Civil society is also present, including, for example, the ICC, the IBA, the European Trade Unions Congress etc.⁹

Something which we also view as extremely important is the establishment of two groups which we hope will assist the Working Group. There is both an academic and practitioners group. More work needs to be done on how these groups will interact with the Working Group itself but what I can say is that it is, at a minimum, very important to the EU that the types of solutions that are looked at in the Working Group are stress-tested by those groups. There is simply too much expertise, practical and academic, not to ensure that this is brought to bear in helping the find the best solution for reforming the current ISDS system.

The EU and the Member States have been actively participating in the discussions and listening to other states' concerns and opinions. We have already learned that we need to widen our focus. For example, some countries favour alternative dispute resolution models and would want to provide for State-to-state dispute settlement mechanisms. Others have raised the issue of the representativeness of the adjudicators, both in terms of geographical representation but also in terms of gender ("pale, male and stale", as the

⁹ See Anthea Roberts who concludes, "UNCITRAL's convening power has been demonstrated: around 100 states and observer entities have been involved in working group meetings so far, along with ten international governmental organizations and several dozen nongovernmental ones." Roberts, Anthea, Incremental, Systemic, and Paradigmatic Reform of Investor-State Arbitration (June 4, 2018). 112 American Journal of International Law (2018). Available at SSRN: <https://ssrn.com/abstract=3189984> or <http://dx.doi.org/10.2139/ssrn.3189984>

line goes). We recognise the importance of these elements and the need to bring them into the deliberations of the Working Group.

5. Conclusions

Let me finish with a few concluding remarks.

The recent past has been a hard time for those of us who believe in multilateralism. If we want international systems to survive in the 21st century, we need to accept that reform may be necessary. For the EU, it is incontrovertible that reform needs to take place in the ISDS regime. This is what the EU is seeking to do.

That reform makes the most sense if it is multilateral. We need to avoid the broken strands of spaghetti, the spaghetti spezzati, that ultimately serve no-one as our world becomes increasingly integrated and connected.

That reform, in our submission, needs at its core to address the issue of permanency. It is only by creating a permanent body that creates predictability and confidence through the expectation that rulings will be issued by independent, highly qualified adjudicators, and will be followed, that we can truly address the concerns associated with ISDS.

That reform can only be built through dialogue and understanding, taking the best of the current system, understanding the concerns held from across the spectrum both in terms of interests and geographically, involving all stakeholders. The EU has started on that

approach and is resolute in its intention to continue in that approach. We hope that you will also be prepared to contribute to these developments.

Thank you.

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