A true reform or mere cosmetic improvements?

Commission proposal for a Multilateral Investment Court

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Summary

T&E has consistently denounced the flawed ISDS mechanism (investor-state dispute settlement). One of the main concerns is that claims by foreign investors, or even threats of claims, could deter the EU or Member States from adopting measures to protect the environment. We, therefore, welcome that the Commission proposes to step away from private, ad-hoc arbitration and establish a multilateral investment court. However, T&E can only give its support to this initiative if our core concerns—most importantly the protection of the right to regulate—are duly addressed.

In recent years, we have seen an alarming increase of states being sued by investors in private arbitration tribunals. In 2016,[i] the total number of claims submitted to international fora such as International Centre for Settlement of Investment Disputes (ICSID) and others was 62—up from 13 in 2000. This fivefold increase is additionally alarming as many claims relate to public interest measures taken by states to protect the environment. This trend has also not gone unnoticed by the public. Countries like Germany saw numerous street protests and an increased interest in investor-state dispute settlement.[ii]

After 97% of the participants at a public consultation rejected the flawed ISDS, the Commission attempted to address the issue. The Commission's TTIP proposal for investment protection indicated a shift towards attempting to appease public outcry with the Investment Court System (ICS) in November 2015.[iii] However, the ICS does not address the core flaws of ISDS. T&E has repeatedly voiced its concern over both systems. Such claims or even a threat of a claim by a foreign investor can lead to a regulatory chill.[iv]

The Commission has taken a step in the right direction in attempting to address citizens' and civil societies' legitimate concerns by intending to abolish the controversial private arbitration and rectify the flaws of ISDS and ICS. The proposal to establish a multilateral investment court (MIC) is certainly a welcome improvement as it will increase transparency and reduce conflicts of interest. However, a number of red lines need to be addressed before the new institution is fit for purpose. At its core, the right to regulate has to be protected and upheld. Substantive rules on investment protection must be improved parallel to setting up the multilateral investment court. The negotiations and ultimately the creation of the multilateral investment court need to be transparent, accountable and impartial.[v] Should the reform fall short of addressing some core concerns related to the protection of public health, animal and plant well-being, the environment, consumers' and labour rights, T&E's support for this new system will be impossible.

For T&E to support the establishment of a multilateral investment court, the following thirteen issues need to be addressed:

1. A truly public process

1.1 A consultation for citizens, not experts

The public consultation is clearly aimed at experts and not the wider public as it does not seek to establish the public's view on whether or not to have a court, but merely on its mechanisms. T&E believes that due to the impact of a new multilateral investment court on citizens, businesses, governments and the European legal order, a public debate on the very necessity to establish a multilateral investment court is essential. We, therefore, call on the Commission to host a legitimate public consultation aimed at understanding the position of citizens.

As it stands, the MIC consultation requires participants to—at the very least—have a good knowledge of European and investment law. The consultation falls short in two areas: questions are highly technical and questions cannot be answered without prior knowledge of the Commission's intentions. In addition, questions are being phrased in very complicated terms lacking clear language.[vi] Nowhere does the Commission outline that the convention establishing a multilateral investment court cannot change jurisdiction and, therefore, the underlying substantive investment protection provisions.

1.2 Transparent negotiations with wide CSO participation

The consultation does not address the question of how negotiations for a convention to establish the MIC would be conducted. These must be fully transparent from the very beginning and open to all stakeholders. Frequent meetings with civil society are key. UNCITRAL and, moreover, the UNFCCC negotiations are good examples of stakeholder participation.[vii] Delegates and negotiators are very approachable and have frequent exchanges with stakeholders.

2. A holistic approach to investment protection

2.1 Safeguard the right to regulate

Claims that the multilateral investment court will not affect environmental decision must be viewed critically. While the multilateral investment court could be an improvement in terms of procedure, substantial provisions on investment are not touched upon, as these are still to be defined within the underlying agreements. This is where the real danger to the environment lies. Any improvements the multilateral investment court may bring will be undermined if substantial provisions on investment in FTAs or BITs (such as fair and equitable treatment (FET)), indirect expropriation and legitimate expectations remain the same as in the previous systems. This gives investors a powerful tool to exercise pressure and sue governments over decisions taken to protect the environment. The past years have seen numerous, highly controversial cases. These include a $4.7 billion claim for compensation following Germany's decision to phase out nuclear energy,[viii] a $1.4 billion claim over permits for a coal-fired plant in Germany[ix] and a currently unknown amount over Romania's refusal to host Europe's largest gold mine.[x]

These examples show that any reform of investment dispute resolution needs to include the pursuit of sustainable development objectives. The Commission must ensure that, in addition to the negotiations and establishment of a multilateral investment court, substantive provisions on investment do not contain the same fundamental flaws as the current provisions on investment protection in FTAs.[xi] As such, protecting the right to regulate via a carve-out clause to protect public policy measures must be introduced in all FTAs.[xii] We propose the following wording: *"Any measure or action undertaken by a Party that aims or has the effect of contributing to a public interest such as environmental protection—including measures or actions combating climate change, social protection, consumer protection and public health protection—does not constitute a breach of the provisions of this Chapter."*[xiii]

2.2 Not losing sight of substantive provisions

While we acknowledge that the Commission cannot create jurisdiction or change substantive provisions during the negotiations for the multilateral investment court, it should make clear that the work of the court and substance of investment protection have to go hand in hand. The Commission must apply a holistic approach to the reform. This process must start as soon as a negotiating mandate is given. The units responsible for the multilateral investment court and the substantive investment protection provisions must work in close collaboration. Without this clear commitment, the initiative is an empty shell and not credible.[xiv]

2.3 Aligning treaties

There is a need for a comprehensive reform which ensures that the same dispute resolution system applies to all—existing and future—investment treaties. It is important that the transition to the multilateral investment court is a key element of all ongoing and future negotiations. The aim would be that, in time, this is the only court mechanism for such disputes and that private arbitration as under ICSID is no longer required.

Bringing all agreements in line is the only way to achieve a real reform of the system and to increase the relevance and credibility of the new court, rather than a simple exercise of expansion. For example, the Energy Charter Treaty needs to be brought under the jurisdiction of the new court. The best way forward is subjecting all investment treaties to the jurisdiction of the multilateral investment court through an opt-in convention. This way, the jurisdiction of the multilateral investment court would apply to all states that have signed the convention and between those states of the convention that have an FTA. The United Nations Mauritius Convention on Transparency for investor-state dispute settlement ("Mauritius Convention") could be a model here.[xv] Individual amendments to existing FTAs do not provide the same certainty as the process can be long or can fail due to a lack of willingness to change the old system.

2.4 Ban treaty shopping

A reform of agreements should also be undertaken to stop so-called 'treaty shopping' whereby investors decide which investment protection system to use to gain maximum financial payout. This misuse of investment provisions by investors has even been identified as a problem by some private arbitration tribunals.[xvi] Investors must not have a range of fora available to them. Only a holistic reform subjecting all agreements to the jurisdiction of the multilateral investment court and disallowing the use of the old ISDS system is acceptable. The reform should—in its core—abolish the flawed ISDS and leave behind private arbitration to the annals of history.

Another problem closely related to ISDS's lack of transparency and having investors chose their most favoured dispute settlement is the practice of out-of-court settlements. Out of 444 concluded ISDS cases by the end of 2015, 26% were settled.[xvii] This does not include cases unknown to the public or settlements that took place before filing a claim. While this is also a common practice in domestic legal systems, it raises serious questions in the context of investment dispute settlement. These out-of-court settlements happen entirely behind closed doors and do not allow third parties to understand the full extent of the settlement. After all, even out-of-court settlements can involve high amounts of public money being spent on compensation and can induce a regulatory chill effect.

3. Ensuring legality and access to justice

3.1 Checking with the CJEU

One of the main problems with the current system is its incompatibility with the Treaties. This issue has been raised by several academics[xviii] and recently the European Parliament.[xix] The EU legal order and powers of the Court of Justice of the European Union (CJEU) are not currently protected. So far, the Commission has not asked the CJEU for an opinion on this pressing issue.[xx] Precautions in current FTAs limiting the powers of arbitration tribunals in relation to domestic law do not sufficiently address the fundamental concerns about the compatibility of the multilateral investment court with EU law. For increased legal certainty, the Commission must, therefore, request the opinion of the CJEU before establishing such a new international court.

3.2 First domestic courts, then international courts

The consultation does not address the exhaustion of domestic legal remedies before obtaining access to the MIC. The exhaustion of domestic remedies is a key principle in international law. It has also found its way into investment law.[xxi] Allowing investors to bypass this principle only perpetuates their privileged status. It is, therefore, important that any convention establishing the multilateral investment court clearly requires the exhaustion of domestic legal remedies before a case can be lodged. After all, domestic courts by their very nature are best suited to interpret and apply national law.[xxii]

3.3 Equal access to justice for individuals

In the past, many arbitration cases concerned environmental decision-making, such as mining or oil exploration projects.[xxiii] Certain investments have had significant impacts on the environment and the population. Yet, it is impossible for individuals to make their voices heard even though these investments have had devastating impacts on water supply and sanitation, air quality, land rights— just to name a few. Furthermore, individuals do not have any possibility to lodge counterclaims in investment tribunals or courts against an investor breaching his responsibilities towards the environment and the local population. This is an unbalanced system running counter to the UN Guiding Principles on Business and Human Rights.[xxiv] Regrettably, the consultation does not seek to address this imbalance. The multilateral investment court still constitutes a separate system for investors only.

One way forward on the procedural level is to allow *amicus curiae* submissions to go further than the UN Commission on International Trade Law (UNCITRAL) transparency rules. Thus, well-founded submissions always have to be accepted and cannot be rejected by the judges. Should submissions be dismissed, a reasoning by the court should be published.

On a substantive level—and thus parallel to the negotiations for the multilateral investment court—we call on the Commission to include meaningful access to justice clauses as required in the Aarhus Convention[xxv] in their FTAs to counterbalance the current one-sided system.

4. Preventing conflict of interest and ensure transparency

4.1 Truly independent judges

A major point of criticism that we raised repeatedly is the lack of judges' independence in the old ISDS and ICS mechanisms.[xxvi] The proposal for the multilateral investment court moves in the right direction to rectify this problem. In order to increase trust and avoid conflicts of interest, judges must be employed full-time and receive a fixed remuneration.

Judges should be selected on a transparent, established and measurable basis. The candidate screening should be carried out by an independent body. The UK Judicial Appointments Commission [xxvii] or the Regional and Judicial Legal Services Commission (RJLSC)[xxviii] for the Caribbean Court of Justice can serve as models.

Judges should have a proven track record in public international law and have experience as a national judge. Moreover, judges must be qualified— besides qualifications in public international and investment law—in areas such as environment, public health, labour rights, consumer protection, human rights, data protection and competition law.[xxix]

Drawing up of the code of conduct for judges needs to be open and transparent. The European Court of Human Rights (ECtHR), Court of Justice of the European Union (CJEU), Caribbean Court of Justice (CCJ) and the WTO have all drawn up codes of ethics, which can serve as models.[xxx]

4.2 Docked or stand-alone court

It is unclear from the initial roadmap and consultation if the multilateral investment court would become a stand-alone institution or docked to existing institutions like the WTO or ICSID. Both options have advantages, but also pitfalls. A stand-alone institution would be truly independent and address the issues of conflict of interest in private arbitration. It can, however, face problems of legitimacy, especially if the number of countries involved is low. On the other hand, docking the multilateral investment court to an existing mechanism would allow the use of pre-established administrative arrangements, thus making a transition easier. However, docking to a mechanism like ICSID carries the risk of falling into old traps and repeating the same mistakes concerning bias and lack of transparency.[xxxi] Given how important this issue is, the Commission should have included this question in the consultation.

4.3 Transparent financing

Any kind of financing of the multilateral investment court, whether or not linked to GDP, FDI or a number of other cases, must be transparent. T&E supports the idea of introducing a user fee for investors when bringing a case against a state. The user fee should be a sufficient high fixed percentage of the investors' claims.

Related to the introduction of user fees, is the need for more stringent rule of third party funding. Wall Street hedge funds heavily invest in ISDS cases hoping for a massive payout in the end.[xxxii] These funds cover the investor s' legal costs in exchange for a cut of the compensation award. Not only does this practice bring about an increase in the number of cases, but it can also lead to a regulatory chill. Governments, which do not have these resources available, will be reluctant to regulate in the public interest due to a fear of a costly compensation claim.

It is, therefore, important that deliberations on the financing of the multilateral investment court take due account of the above practice and introduce a system that discourages investors from bringing a claim.

5. No correlation between FDI and investment resolution

The question whether investment resolution ultimately improves the global investment climate and increases foreign direct investment (FDI) is controversial. Academic studies are inconclusive on the precise correlation between investment dispute resolution and increased FDI. Several studies suggest that the effect is marginal.[xxxiii] It is, therefore, misleading to argue that the multilateral investment court would positively contribute to the investment climate.

Conclusions

The pressure of civil society forced the Commission to rethink its approach to ISDS and resulted in a reform proposal such as ICS and the current multilateral investment court. The added valued of such a court is that it puts an end to the controversial ISDS and renders the system more transparent and accountable.

A true reform needs, first and foremost, to ensure that the substance of investment protection provisions is overhauled. The right to regulate must be adequately safeguarded. The old ISDS mechanism must be completely abolished by ensuring investors cannot have recourse to it in the future.

Secondly, the whole process of negotiations, establishment, financing and appointment of judges must be transparent. This includes constant exchange with civil society on these matters and having a truly public consultation.

Thirdly, the relationship between domestic courts, individuals and the multilateral investment court needs to be clarified. An opinion of the CJEU on the compatibility of such a court with the EU legal order is key. Individuals must be given meaningful access to justice.

Finally, the inconclusive relationship of increased FDI through investment dispute settlements needs to be demystified.

T&E's support for the establishment of the multilateral investment court is conditional upon the Commission addressing these core concerns set out in this paper. By failing to address these concerns, we will not be able to support this initiative further. T&E will continue to closely monitor the process—including the impact assessment, the negotiating mandate and the negotiations itself—in order to ensure a true reform of the system instead of mere cosmetic improvements.

Further information

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Endnotes

[i] Figures taken from UNCTAD Investment Policy Hub available at http://investmentpolicyhub.unctad.org/ISDS (retrieved 10 March 2017)
[ii] Hundreds of thousands protest in Berlin against EU-U.S. trade deal available at http://www.reuters.com/article/us-trade-germany-ttip-protests-idUSKCN0S40L720151010 (retrieved 13 March 2017).
[iii] The ICS reforms have also been incorporated in CETA and the EU- Vietnam FTA.
[iv] T&E contribution to 2015 ISDS consultation, July 2014 available at https://www.transportenvironment.org/publications/tes-submission-commissions-public-consultation-isds (retrieved 21 February 2017) Joint Analysis of CETA's Investment Court System by T&E, BEUC, Client Earth,

EEB and EPHA, June 2016 available at https://www.transportenvironment.org/publications/joint-analysis-ceta%E2%80%99s-investment-court-system-ics (retrieved 21 February 2017)

[v] T&E feedback to roadmap on the establishment of a multilateral investment court, September 2016 available at https://www.transportenvironment.org/publications/establishment-multilateral-investment-court-investment-dispute-resolution (retrieved 24 February 2017)

[vi] An example would be question 27.

[vii] The Handbook on the United Nations Framework Convention on Climate change states that " seeking contributions and public participation from all stakeholders and encouraging their participation in the negotiation process" is an important component of the negotiations available at https://unfccc.int/resource/docs/publications/handbook.pdf (retrieved 9 March 2017)

[viii] Vattenfall AB and others v. Federal Republic of Germany (II) ICSID Case No. ARB/12/12

[ix] Vattenfall AB, Vattenfall Europe AG, Vattenfall Europe Generation AG v. Federal Republic of Germany (I) ICSID Case No. ARB/09/6

[x] "Rosia Montana" Gabriel Resources v. Romania ICSID Case No. ARB/15/31, pending

[xi] Investment is covered in Chapter 8 CETA, Chapter 9 Singapore and Chapter 8 Vietnam

[xii] Joint Analysis of CETA's Investment Court System by T&E, BEUC, ClientEarth, EEB and EPHA, June 2016 https://www.transportenvironment.org/publications/joint-analysis-ceta%E2%80%99s-investment-court-system-ics (retrieved 21 February 2017)

[xiii] This carve- out has been jointly drafted by T&E, BEUC, Client Earth, EEB and EPHA.

[xiv] See also point on the right to regulate above.

[xv] United Nations Mauritius Convention on Transparency for Investor- State- Dispute Settlement http://www.uncitral.org/pdf/english/texts/arbitration/transparency-convention/Transparency-Convention-e.pdf (retrieved 23 February 2017)

[xvi] Saluka Investments B.V. v. the Czech Republic, UNCITRAL Partial Award, 17 March 2006; Mobil v. Venezuela Decision on Jurisdiction, 10 June 2010, ICSID Case No. ARB/07/27

[xvii] UNCTAD IIA Issue Note No.2 June 2016 available at http://unctad.org/en/PublicationsLibrary/webdiaepcb2016d4_en.pdf (retrieved 14 March 2017)

[xviii] Professor Dr. Inge Govaere, Director of the European Legal Studies Department of the College of Europe, Bruges, "TTIP and Dispute Settlement: Potential Consequences for the Autonomous EU Legal Order", Research Paper in Law 01 / 2016 available at https://www.coleurope.eu/research-paper/ttip-and-dispute-settlement-potential-consequences-autonomous-eu-legal-order (retrieved 31 January 2017; Advocate General Kokott and Christoph Sobotta, "Investment Arbitration and EU law", Cambridge Yearbook of European Legal Studies, Volume 18, December 2016, pp. 3-19 available at https://www.cambridge.org/core/journals/cambridge-yearbook-of-european-legal-studies/article/div-classtitleinvestment-arbitration-and-eu-lawdiv/96D57753C361BD22F35D37BE6EE9CC5D (retrieved 31 January 2017)

[xix] Motion for a resolution B8-1220/2016 seeking an opinion from the Court of Justice on the compatibility with the Treaties of the proposed agreement between Canada and the European Union on a Comprehensive Economic and Trade Agreement (CETA) (2016/2981(RSP), 11 November 2016

[xx] In Opinion 2/15 the Commission did not request the Court resolve the issue of compatibility of ISDS in the EU- Singapore FTA, although the Court already had given an opinion in a similar matter in 1/13 on the accession to the ECHR. AG Sharpston in para. 85 of her opinion clarified that the Court would not consider questions of compatibility.

[xxi] Art. 26 ICSID Convention: "Consent of the parties to arbitration under this Convention shall, unless otherwise stated, be deemed consent to such arbitration to the exclusion of any other remedy. A Contracting State may require the exhaustion of local administrative or judicial remedies as a condition of its consent to arbitration under this Convention." retrieved from https://icsid.worldbank.org/en/Documents/icsiddocs/ICSID%20Convention%20English.pdf (retrieved 31 January 2017)

[xxii] Vattenfall also lodged a case with the German Constitutional Court. BVerfG, Judgment of the First Senate of 06 December 2016 - 1 BvR 2821/1

[xxiii] Chevron v. Ecuador (I), PCA Case No. 34877, 31 August 2011; "Rosia Montana" Gabriel Resources v. Romania No. ARB/15/31, pending

[xxiv] UN Guiding Principles on Business and Human Rights from http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf (retrieved 2 February 2017)

[xxv] Art 9 reads: "Each Party shall, within the framework of its national legislation, ensure that any person who considers that his or her request for information under article 4 has been ignored, wrongfully refused, whether in part or in full, inadequately answered, or otherwise not dealt with in accordance with the provisions of that article, has access to a review procedure before a court of law or another independent and impartial body established by law. "[...] Aarhus Convention available at http://www.unece.org/fileadmin/DAM/env/pp/documents/cep43e.pdf (retrieved 27 February 2017)

[xxvi] Joint Analysis on ICS in CETA

[xxvii] Judicial Appointments Commission https://jac.judiciary.gov.uk/ (retrieved 21 February 2017)

[xxviii] For more information on the RJLSC see http://www.caribbeancourtofjustice.org/about-the-ccj/rjlsc-2 (retrieved 21 February 2017)

[xxix] The US and Japan have both emphasised their interest in appointing judges with an expertise relevant to the dispute in question. See Presentation by David Gaudkrodger, Investment Division, OECD on Adjudicators' Qualifications: Independence and Neutrality, 14 December 2016

[xxx] CJEU Code of Conduct available at http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:C:2016:483:FULL&from=FR; ECtHR Resolution on Judicial Ethics available at http://www.echr.coe.int/Documents/Resolution_Judicial_Ethics_ENG.pdf; CCJ Code of Judicial Conduct available at http://www.caribbeancourtofjustice.org/papersandarticles/ccj-code%20of%20conduct.pdf and WTO Rules of Conduct available at https://www.wto.org/english/tratop_e/dispu_e/rc_e.htm (retrieved 10 March 2017)

[xxxi] The president of the World Bank is the chairman of the ICSID Administrative Council.

[xxxii] Paul Keenlyside, When You Thought Trade Deals Could Not Get Any Worse -- Enter Wall Street available at http://www.sierraclub.org/compass/2016/12/when-you-thought-trade-deals-could-not-get-any-worse-enter-wall-street (retrieved 27 February 2017)

[xxxiii] Axel Bergera , Matthias Busseb , Peter Nunnenkamp , and Martin Roy, More Stringent BITs, Less Ambiguous Effects on FDI? Not a Bit!, Staff Working Paper ERSD-2010-10, WTO Economic Research and Statistics Division available at https://www.wto.org/english/res_e/reser_e/ersd201010_e.pdf (retrieved 27 February 2017); Shiro Patrick Armstrong, Luke R. Nottage The Impact of Investment Treaties and ISDS Provisions on Foreign Direct Investment: A Baseline Econometric Analysis
Sydney Law School Research Paper No. 16/74 available at https://papers.ssrn.com/sol3/papers2.cfm?abstract_id=2824090 (retrieved 27 February 2017)