European Federation for Investment Law and Arbitration
(EFILA)

A response to the criticism against ISDS

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**Disclaimer**

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Introduction

Since the Lisbon Treaty entered into force almost 6 years ago, the European Commission began developing its own EU investment policy. The core of this new investment policy is the conclusion of trade and investment treaties with strategically important countries. In the context of these negotiations, the critique against investor-state dispute settlement (ISDS), which is contained in practically all Bilateral Investment Treaties (BITs) as well as in recently concluded Free Trade Agreements (FTAs) such as the EU-Canada treaty (CETA) and the EU-Singapore treaty, has become more vocal.

More specifically, since June 2013, the European Union (EU) and the United States of America (USA) have been negotiating the Transatlantic Trade and Investment Partnership (TTIP) Agreement, the first preferential trade and investment agreement between the two dominant economic players worldwide. The European Commission is negotiating the agreement on the basis of negotiating directives issued by the Council and it consults simultaneously with governments, members of the European Parliament and civil society throughout the process. The defenders of TTIP argue that the agreement would result in multilateral economic growth,¹ while its critics claim that it would increase corporate power houses and make it more difficult for governments to regulate markets for public benefit.²

Most EU Member States and the US³ are in favour of including this type of dispute resolution mechanism as they consider that ISDS will encourage investment flows.⁴ The European Commission argues that ISDS helps to attract and moreover maintain US FDI in the EU and, therefore, needs to be included in the trade agreement.⁵ However, some

¹ See in particular the EC’s impact assessment regarding the benefits of TTIP: http://europa.eu/rapid/press-release_MEMO-13-211_en.htm; see also: “This EU-US trade deal is no ‘assault on democracy’” by Ken Clarke at the guardian, Monday 11 November 2013, available at: http://www.theguardian.com/commentisfree/2013/nov/11/eu-us-trade-deal-transatlantic-trade-and-investment-partnership-democracy.n
² See e.g., “This transatlantic trade deal is a full-frontal assault on democracy”, by George Monbiot, at the guardian, Monday 4 November 2013, available at: http://www.theguardian.com/commentisfree/2013/nov/04/us-trade-deal-full-frontal-assault-on-democracy
³ US President Obama has recently repeatedly underlined the importance of ISDS in TTIP and TPP, see e.g., https://www.yahoo.com/politics/why-obama-is-happy-to-fight-elizabeth-warren-on-118537612596.html; http://www.washingtonpost.com/blogs/plum-line/wp/2015/04/27/is-ppp-trade-deal-a-major-giveaway-to-major-corporations-an-exchange-between-obama-and-sherrod-brown/
⁴ Also, according to some commentators, the investment provisions of TTIP are meant to be “a blueprint for any future investment agreement with countries whose investment climate is less stable than the one in Europe and the United States” and thus the basis for a global investment protection framework, not limited to regional purposes, see Global Policy, More than Regional Investment Protection – ISDS in the EU-US trade agreement, by Jana Höffken - 6th May 2014, available at: http://www.globalpolicyjournal.com/blog/08/05/2014/more-regional-investment-protection-%E2%80%93-isds-eu-us-trade-agreement
radical critics see it as a "Trojan horse" enhancing the power of US companies at the expense of national sovereignty and interests. In an attempt to appease the critics, the European Commission has paused the negotiations on ISDS for a few months and launched a public consultation on the topic. EFILA has participated in this consultation.

Critics have raised concerns about the pro-investor interpretation of investment treaty provisions and their perceived unpredictability, the alleged lack of transparency of arbitral proceedings, the alleged lack of independence and impartiality of arbitrators. Others have suggested that ISDS bypasses the operation of domestic law and national courts and stymies the right of states to regulate. Criticisms have also been raised against the investor-state arbitration process itself, claiming that it allows partisan, self-interested arbitrators to secretly overrule governments with no right of appeal.

Consequently, the European Federation for Investment Law and Arbitration (EFILA), a recently established non-profit think tank bringing together a significant amount of practical experience in investment law and arbitration, decided to write this paper in order to address the most often voiced myths against ISDS.

This paper aims at balancing the currently rather one-sided debate by providing an in-depth analysis, based on arbitration practice and literature. It is divided in the following 11 main criticisms, each of which are subdivided into further specific issues.

**Executive summary**

- Criticism 1 concerns the claim that the substantive treaty provisions are interpreted in favour of investors, whereas the statistical evidence shows that respondent States in arbitral proceedings consistently win more cases than the investors who bring claims against States;
- Criticism 2 addresses the argument that perceived inconsistency and unpredictability of arbitral decisions, but the reality is that by their very nature investment disputes are fact- and case specific and so is their resolution;
- Criticism 3 deals with the claim of a lack of transparency, but the truth is that the majority of arbitral proceedings take place under ICSID rules and the ICSID awards have been published on the ICSID website for several years and the new UNCITRAL Transparency Rules introduce the same level of transparency for UNCITRAL proceedings;
- Criticism 4 concerns the perceived lack of independence and impartiality of arbitrators, however, the current system of investment arbitration already

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8 See EFILA website: [www.efila.org](http://www.efila.org). EFILA also submitted its observations to the UK BIS Committee inquiry on TTIP. This submission is also available on the EFILA website.
includes effective control mechanisms to ensure that any lack of independence or impartiality can be tackled by both States and investors;

- Criticism 5 relates to the claim that a small elite group handles most arbitrations, but the truth is that arbitrators are appointed by States and investors and thus States are entirely free to appoint other individuals thereby widening the pool of arbitrators;

- Criticism 6 addresses the claim that investment disputes lead to a diversion of public money from public goods and services, whereas there is no evidence that the domestic judicial system is cheaper;

- Criticism 7 deals with the argument that ISDS leads to so-called "regulatory chill" but there is no evidence which would support such a claim;

- Criticism 8 concerns the claim that ISDS allows international companies to bypass national judicial systems, whereas the truth is that international arbitration is the most efficient way to handle investment disputes;

- Criticism 9 deals with the argument that since both the US and the EU have highly evolved, efficient Rule of law legal systems, ISDS is not necessary in TTIP, however since TTIP will serve as model for other investment treaties a modern ISDS chapter must be included;

- Criticism 10 concerns the argument that when governments concede to demands for ISDS provisions, they may be less willing to agree to other reforms such as greater market access, however, the CETA shows that creative solutions can be found;

- Criticism 11 addresses the claim that despite the absence of investment treaties, flows of FDI go into Brazil and other emerging economies, apparently showing that there is no positive correlation between FDI flows and investment treaties, however, the truth is that investment treaties are one instrument of many which States use to attract FDI;
Criticism 1: Pro-investor interpretation of substantive treaty protections.

a) Pro-investor interpretation of investment treaties.

1.1. To verify the validity of the argument that arbitral tribunals apply a broad pro-investor interpretation of substantive protection provisions, it would be necessary (at least at an initial stage of research) to implement a quantitative and qualitative analysis of investment arbitration final awards “favouring” the investor on the merits. From the outset, it is important to make some (general) language differentiations; an award decided in favour of the State is an award in which the investor’s claims are dismissed and/or a counterclaims are successful, an award decided in favour of the investor is an award in which the investor’s claim wins on the merits and is entitled to payment and/or compensation, and a pro-jurisdiction award is an award where the tribunal finds jurisdiction but without deciding on the merits of the dispute. Some literature has tried to argue that by making a finding of jurisdiction, this somehow is in favour of the investor. However, there is no causal link between a finding of jurisdiction and an arbitral tribunal ultimately being pro-investor on the merits of the case.

1.2. For example, in 2012 ISDS was strongly criticized as a pro-investor system of corporate rights. However, UNCTAD stated in its annual World Investment Report of 2014 that “arbitral developments (...) brought the overall of concluded cases to 274”. Of these, approximately 43% of cases were decided in favour of the State, 31% in favour of the investor and 27% were settled. The 2014


UNCTAD statistics reveal that from 100 % of the cases where the tribunal found jurisdiction more were resolved in favour of States than investors, which would suggest that a pro-investor interpretation is not applied to substantive protections, otherwise this would have been reflected on the number of final awards decided in favour of the investor. Conversely, one could argue that ISDS provides for a stable balance between the protection of investors and the protection of States' regulatory powers. Indeed, **UNCTAD figures confirm that States continue to win more cases than investors**, thus the pro-investor argument is unfounded. This is also confirmed by the latest ICSID statistics (2015-1), which show that only 46% of all ICSID awards upheld claims in part or in full, while **53% of the claims were dismissed** either for lack of jurisdiction or on the merits. 1% of the claims were manifestly without legal merit.\(^\text{11}\) At the very least, outcomes of all known investment arbitration cases indicate that by the end of 2013 arbitral tribunals were in most cases ruling not in favour of investors, but rather in favour of States which are respondent in arbitral proceedings.

1.3. The above statistics serve only to dispel the claim that the majority of investment cases are decided in favour of the investor. In this regard it is worth highlighting that the measure of whether arbitral tribunals are fair or pro-investor cannot be conclusively ascertained by looking at the percentages won. Critics of the system who focus on the numbers of cases won or lost are masking the more vital question: Are investors winning more cases than they should win, because ISDS is somehow canted in their favour? Such a question cannot be objectively determined through statistics.

1.4. In addition it should be noted that, the authority of tribunals is prescribed in the investment treaties and may only go as far as the intention of the drafters of investment treaties (i.e. the States). State sovereignty is a fundamental principle (peremptory norm) of international law codified in Article 2(1) of the Charter on the United Nations.\(^\text{12}\) From this follows that States cannot be subjected to jurisdiction without their consent,\(^\text{13}\) in particular this holds true with regard to (investment) arbitration.\(^\text{14}\) Arbitral tribunals are not free to expand their authority beyond the boundaries prescribed by investment treaties.

1.5. Moreover, critics fail to mention the fact that the system of investment arbitration has been created not by business or big international corporations, but by sovereign States, which understand that without legal stability and an

\(^{11}\) ICSID statistics 2015-1, available at: [https://icsid.worldbank.org/apps/ICSIDWEB/Pages/News.aspx?CJD=42&ListID=74f1e8b5-96d0-4b0a-8f0c-2f3a92d84773&variation=en_us](https://icsid.worldbank.org/apps/ICSIDWEB/Pages/News.aspx?CJD=42&ListID=74f1e8b5-96d0-4b0a-8f0c-2f3a92d84773&variation=en_us), accessed 16 February 2015.


\(^{13}\) ‘[...] the general consent of states creates general rules of application[...]' in Ian Brownlie, Principles Of Public International Law, OUP 2018, p. 4

effective framework of protection for international investors and their investments flows of foreign direct investments (FDI) will significantly diminish.\textsuperscript{15} This is why the two international instruments which provide for investors’ protection and for recourse to international arbitration against State’s wrongful measures, the ICSID Convention and the New York Convention,\textsuperscript{16} are among the most successful international commercial treaties, signed respectively by 159 and 150 States.

1.6. Furthermore, it is not a coincidence that most currently existing IIAs contain very broad definitions of protected investments and investors as well as broad provisions describing substantive levels of protection (fair and equitable treatment, direct expropriation etc.). States realize that by broadening the scope of the protection of investors and investments they increase their chances of attracting FDI. It is not a broad and creative interpretation by arbitral tribunals, which expands the field of investment arbitration, but precisely the consciously broad wording of IIAs, which constitute boundaries for arbitral tribunals. In other words, based on a calculation of advantages offered by the IIAs, i.e. greater flow of FDIs, it has been a conscious decision of State parties to IIAs to include very broad language which provides protection to all imaginable investments and investors. The validity of this approach has been confirmed by a recently published study of the Dutch Statistical office which shows that FDI flows increase by 35\% after ratification of a BIT.\textsuperscript{17} Of course, States are equally able to limit the scope of protected investors and investments in future IIAs. Indeed, we can observe this trend in relation to the treaties signed or currently negotiated by the EU (CETA and TTIP).

b) **Available means of interpretation**

1.7. Moving from case outcomes to legal content analysis, so far there is no qualitative research to prove a pro-investor expansive approach on issues of legal interpretation of substantive standards\textsuperscript{18}.

1.8. The claim that ISDS arbitrators are pro-jurisdiction does not find empirical support. Critics who support this claim often use the argument that arbitrators have a monetary incentive to find jurisdiction. However, according to publicly available official U.S. and Canadian Statistics ISDS arbitrators decline jurisdiction.

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\textsuperscript{16} The New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.


\textsuperscript{18} Van Harten: “Notably, the coded issues were limited to questions of jurisdiction and admissibility and did not include, for example, substantive standards or procedural issues” (see fn. 9).
more often than US and Canadian Federal judges, who have lifetime tenure and a fixed salary. The implied “self-interest” argument of tribunals in finding jurisdiction is therefore unsubstantiated. Moreover, there are serious computation problems with critics’ studies purportedly supporting the assertion that ISDS arbitrators uphold their jurisdiction more often than can be explained by the jurisdictional issues on which they are ruling. For example, if one takes the repeat arbitral decisions against Argentina out of the equation, the ISDS jurisdictional numbers are nowhere near as interesting. Lastly, the existing differences regarding treaty texts, jurisdictional language etc. must be taken into account in any empirical study.

1.9. Previous analysis on diversity and harmonization of treaty interpretation has found that there is no preferable method of treaty interpretation. In particular, there are no findings proving a preference for expansive interpretation of substantive protections, but rather a diversified system using a wide range of treaty interpretation mechanisms depending on the specific needs of the case in dispute. Due to the broad substantive protections granted to investors in BITs, arbitral tribunals have sought to rely on restrictive, expansive and neutral interpretation techniques commonly known in the international public law sphere.

1.10. For example, a restrictive approach has been used when arbitral tribunals have found ambiguity in the scope of umbrella clauses. Tribunals tend to choose a more conservative and prudential approach under the principle of “in dubio pars mittor est sequenda” (SGS v Pakistan and Noble Ventures v Romania). Equally, some tribunals have embraced an “expansive” interpretative method in accordance with the object and purpose of the BIT, which is “to create and maintain favorable conditions for investments by investors of one Contracting Party in the territory of the other”. Given that the intention of States in negotiating and creating BITs is to create a broad framework to attract FDI, it is somewhat difficult to argue that an expansive approach is favourable for the investor, since arbitral tribunals are only interpreting treaty provisions in line with the States’ express intention at the time of the BITs’ creation.

1.11. All IIAs, as treaties signed by two or more states, are governed by public international law. Therefore, the point of departure for all arbitral tribunals to interpret IIAs is the Vienna Convention on the Law of Treaties of 1969 (VCLT), an instrument concluded by most States in the world and reflecting customary

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20 SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan, ICSID Case No. ARB/01/1 and Noble Ventures, Inc. v. Romania, ICSID Case No. ARB/01/11.
21 SGS Société Générale de Surveillance S.A. v. Republic of the Philippines, ICSID Case No. ARB/02/6, See also Eureko B.V. v. Republic of Poland.
international law. As correctly pointed out in a recent study prepared at the request of the European Parliament\textsuperscript{23}:

'[b]y abandoning the methodology of interpretation enshrined in the Vienna Convention on the Law of Treaties the tribunals would free themselves from the bonds of their masters, i.e. the state parties to the investment treaties.'\textsuperscript{24}

1.12. In fact, arbitral tribunals in investment cases always rely on means of interpretation provided in Article 31 (General rule of interpretation) of the VCLT. Sometimes, but very rarely, tribunals also rely on Article 32 which provides supplementary means of interpretation. Article 31 of the VCLT provides that

"[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

1.13. Article 32 VCLT further clarifies that the context of a treaty should comprise, \textit{inter alia}, its text, preamble, annexes and other documents prepared in connection with the conclusion of the treaty or documents accepted as such by the parties. The purpose and object of all IIAs, usually found in preambles,\textsuperscript{25} is encouragement and reciprocal protection of investments.\textsuperscript{26} Accordingly, \textit{prima facie}, the perception may arise that the interpretation of broad provisions of the IIAs may be favourable for investors.\textsuperscript{27} However, despite such broad language included in preambles and the treaties itself, many arbitral tribunals chose to follow "a balanced approach to the interpretation of the Treaty's substantive provisions for the protection of investments",\textsuperscript{28} Furthermore, as indicated by UNCTAD in its most recent World Investment Reports, many of the most recently concluded IIAs contain in their preambles sustainable development-oriented features which are further supplemented by "treaty elements that aim more broadly at preserving regulatory space for public policies of host countries and/or at minimizing exposure to investment arbitration."\textsuperscript{29}

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\textsuperscript{24} \textit{Ibid.}, p. 69-70.

\textsuperscript{25} Christoph H. Schreuer "Diversity and Harmonization of Treaty Interpretation" [2006] TDM 2.


\textsuperscript{29} UNCTAD, World Investment Report 2014.
\end{flushright}
1.14. Moreover, sometimes in their reasoning arbitral tribunals review past decisions related to similar provisions found in other IIAs in order to arrive at their own judgment. However, as the principle of precedent does not exist in international law, it is claimed that this may lead to inaccurate decisions which disregard the actual intention of the state parties to the particular treaty under consideration. On this basis, critiques recommend that the ISDS system should be reformed and that there should be an appeal mechanism system to ensure that states remain masters of their treaties or that states should be able to issue a binding interpretation of provisions of the treaties. This conclusion not only fails to recognize that international courts and tribunals, such as the International Court of Justice itself, often rely on their past decisions. It also fails to recognize the fact that the State parties when creating the ISDS system have already established a necessary system of checks and balances in order to protect them from the creative interpretation of arbitral tribunals. The ultimate sanction imposed by the ISDS system on arbitral tribunals for failure to respect the limits imposed on it by State parties to the investment treaties is annulment of the awards. Indeed, States have successfully used the annulment procedure. Nevertheless, it is recognized by many practitioners of investment arbitration that the annulment system as currently designed has some shortcomings and should be improved.

c) Conclusion

1.15. To conclude, it is important to differentiate between arbitral tribunals being pro-investor and arbitral tribunals being pro-jurisdiction. Some have tried to suggest that by making a finding of jurisdiction, arbitral tribunals are somehow favouring investors. However, there is no causal link between a finding of

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31 Pieter Jan Kuijper et. al., supra note 23, p. 67: ‘Hence, creating `consistency` by a `de facto precedent system` which sidesteps the primary means of interpretation comes at great costs. By abandoning the methodology of interpretation enshrined in the Vienna Convention on the Law of Treaties the tribunals would free themselves from the bonds of their masters, i.e. the state parties to the investment treaties.’.
32 Ibid., p. 69-70.
33 ICJ, Land and Maritime Boundary between Cameroon and Nigeria (Preliminary Objections), ICJ Rep. 1998, 275, 292, para. 28: ‘It is true that, in accordance with Article 59, the Court’s judgments bind only the parties to and in respect of a particular case. There can be no question of holding Nigeria to decisions reached by the Court in previous cases. The real question is whether, in this case, there is cause not to follow the reasoning and conclusions of earlier cases.’.
34 As of 31 December 2013, fifty ICSID annulment proceedings were concluded, and eleven proceedings were pending, the ICSID CASELOAD – STATISTICS (ISSUE 2014-1), available at: https://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=CaseLoadStatistics, accessed 16 February 2015.
jurisdiction and an arbitral tribunal ultimately being pro-investor on the merits of the case. An accurate method of assessment (to verify if arbitral tribunals have a very broad pro-investor interpretation of substantive protections) should rather be based on the outcome of final awards deciding on the merits.

1.16. In reality, UNCTAD statistics have showed that 53% of the final awards (or awards on the merits) have favoured States. These figures confirm that States continue to win more cases than investors, thus strongly suggesting that the pro-investor argument is unfounded. Finally, there is no room to argue that ISDS is an asymmetrical system between the investor and the State hosting the investment. The very own nature of the ISDS mechanism is to grant to its different participants a main role in different stages. While States have created certain conditions for foreign investors, these investors are then entitled to use these conditions to protect themselves from an alleged BIT breach.

*Criticism 2: Divergent interpretation of similar or identical IIA provisions: inconsistency and unpredictability of decisions*

2.1 Other critics complain that even though many IIAs contain very similar or identical provisions, investment tribunals tend to interpret them differently from case-to-case. This, critics say, precludes the emergence of a consistent body of law.

2.2 International investment law is not based on one multilateral treaty but rather on a web of investment treaties. There are over 3000 BITs, FTAs and other similar instruments designed to foster international trade and protect foreign investors and their investments. These instruments have been negotiated between different parties, no doubt a reflection of a State’s preference to tailor make their treaties.

2.3 The decisions of investment tribunals are based largely on bilateral treaties implemented by ad hoc, one-off, tribunals. Furthermore, these tribunals are bound to apply the substantive rules on a case by case basis. This clearly is a significant limitation of convergence.

2.4 Furthermore, it has to be recalled that the system of a binding precedent is foreign to the system of public international law. Similarly, to investment tribunals, judgments of the ICJ have no binding force except between the parties and in respect of the particular case.\(^{36}\) Even if the system of precedent were incorporated into the system of international law, tribunals would not be able to fully rely on the interpretation of similar or identical provisions by other

\(^{36}\) *Statute of the International Court of Justice* Article 59.
tribunals as the parties’ intent and negotiating history differ from treaty to treaty.

2.5 This reality has long been recognized by investment arbitral tribunals and other tribunals, as confirmed by a tribunal in *Methanex Corporation v. United States of America* case:

> ‘As to the third general principle, the term is not to be examined in isolation or in abstracto, but in the context of the treaty and in the light of its object and purpose. One result of this third general principle, being relevant to Methanex’s first argument on GATT jurisprudence and Article 1102 NAFTA, is that, as noted by the International Tribunal for the Law of the Sea in The MOX Plant case (as also applied in The OSPAR case): “the application of international law rules on interpretation of treaties to identical or similar provisions of different treaties may not yield the same results, having regard to, inter alia, differences in the respective contexts, objects and purposes, subsequent practice of parties and travaux préparatoires.”’

2.6 The facts of the cases decided by arbitral tribunals in investment disputes, even though similar, differ substantially, and at least as much as the economic and political realities differ between those sovereign States which signed the investment protection agreements. In other words, by their very nature investment disputes are bred from diverging realities and so this is sometimes reflected in the resolutions by arbitral tribunals—When arbitral tribunals sometimes arrive at diverging views and different interpretations one should not regard it as a failure of the system but rather as a reminder that by its nature the system is fragmented.

**Conclusion**

2.7 In the absence of a multilateral investment treaty to regulate the entire body of investment law some divergences in treaty interpretations are a natural consequence of the system. A system which over the past years has nonetheless produced a fairly robust body of investment case law. Based on this case law, it can instead be argued that in spite of the web of broadly similar but not identical treaties on which investment law is based, there is still a high degree of consistency amongst tribunal decisions.

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38 The MOX Plant case (Ireland v. United Kingdom), Order on Provisional Measures, 3rd December 2001, para. 51 (available at: [https://www.itlos.org/fileadmin/itlos/documents/cases/case_no_10/Order.03.12.01.E.pdf](https://www.itlos.org/fileadmin/itlos/documents/cases/case_no_10/Order.03.12.01.E.pdf)).
Criticism 3: Lack of transparency in investment disputes

a) Introduction

3.1 Investment arbitration is continually evolving and the question of Transparency of the arbitral process is no exception. Transparency has also been a principle under development for the last 20 years of the ISDS system, which has been taken into account for a long time as an evolving principle of the investment arbitration practice in its different expressions (i.e. CAFTA-DR, NAFTA, Amicus Curiae and Third party rights, etc.)\(^{39}\). Transparency has evolved into its new role by positioning itself as one of the global norms in international investment law by means of the 2014 UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration, which has been adopted by the UN as the UN Convention on transparency for investor-state dispute resolution. In addition, it is important to understand that the confidentially principle in arbitration is not equal to a lack of transparency; lack of transparency would mean that investment arbitration is not an accountable system. This is an unfounded criticism since investment treaty arbitration contains a number of different control mechanisms to ensure accountability\(^ {40}\). Moreover, access to investment arbitration practice can be easily done by the numerous contributions of legal scholarship on the subject and through case law publications and databases; both sources play an important role for the transparency and accountability of investment treaty disputes.

b) Transparency in CAFTA, NAFTA and ICSID 2006 Amendments

3.2 Practice of transparency in Investor-State Arbitration can be seen in CAFTA and NAFTA provisions, which allow non-disputing party participation. This Free Trade practice arose due to the fact that despite arbitral awards having confined and binding effects\(^ {41}\) only on the disputing parties, other non-disputing State Parties can have the opportunity to influence in the treaty interpretation analysis of future awards.

3.3 For example, Article 10.20.2 of the Dominican Republic–Central America–United States Free Trade Agreement (CAFTA-DR) includes the possibility of a non-disputing State Party (but CAFTA signatory\(^ {42}\)) to participate in an on-going investor-State arbitration case, by submitting its opinion on issues of treaty interpretation that arise in that specific case. For this purpose, CAFTA Article

\(^{39}\) ICSID Rule 32(2) and Rule 37.

\(^{40}\) For example, in the case of ICSID self-contained system according to Rule 50 (1)(c)(3) an award can be annulled if the Tribunal was not properly constituted; that the Tribunal has manifestly exceeded its powers; that there was corruption on the part of a member of the Tribunal; that there has been a serious departure from a fundamental rule of procedure; that the award has failed to state the reasons on which it is based.


10.21 obliges the Respondent (State Party) to transmit certain documents in relation to the arbitral procedure to the non-disputing Parties which permits them to become fully informed on the issues of that case before submitting its briefing to the tribunal (*Commerce Group Corp. and San Sebastian Gold Mines, INC v. El Salvador*).

3.4 **CAFTA provisions on the participation of non-disputing State party** were influenced by the NAFTA practice. Article 1128 NAFTA was the first treaty provision stipulating the right to make submissions by a non-disputing State Party, which has been invoked in many NAFTA cases (*Pope & Talbot Inc. v Canada, Methanex Corp. v United States and UPS Inc. v Canada, Mobil v Canada, ADF v United States, Bayview Irrigation et.al v Mexico, Chemtura Corp v Canada et.al*). Overall, the CAFTA and NAFTA practice of allowing participation of a non-dispute State Party into an arbitral proceedings dismisses the argument of lack of Transparency in investment arbitration. Conversely, it illustrates the efforts investment law has made in pursing Transparency in many and diverse ways, by monitoring not only pending cases but also by influencing and submitting opinions on issues affecting treaty interpretation of further disputes.

3.5 In 2006, ICSID's rules were amended in order to make non-dispute parties able to intervene in arbitration proceedings and attend hearings. The new rules also promote disclosure of ICSID awards. The participation on third non-disputing parties has incorporated into ISDS a different way of promoting transparency by means of public interest participation (*see below*). The other relevant amendment is in ICSID Rule 48, where the Centre shall promptly include in its publications excerpts of the legal rules applied by arbitral tribunals. The aim of this amendment is to give access to the public to the legal reasoning of the Tribunals. This amendment to Rule 48 contributes to the construction of public case law and that in turn serves not only to provide persuasive reasoning for future ICSID tribunals but also ensures arbitral tribunals are subject to public scrutiny.

c) **Amicus Curiae**

3.6 **Amicus Curiae** (meaning “friend of the court”) is where a voluntary third party seeks to participate in a specific investment arbitration dispute in order to provide a neutral and a well supported opinion regarding an issue of public concern. Mostly, *amicus* participants in investment arbitration have been NGOs, and arbitral tribunals have recognised the important value of the *amicus* briefs, highlighting that in addition to representing civil society, an amicus should demonstrate how its background, experience, expertise and special perspectives can assist in the particular case (*Suez, Sociedad General de Aguas de Barcelona*).

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44 Briefs are accepted under general power of ICSID Convention Article 44.
S.A., and InterAguas ServiciosIntegrales del Agua S.A v Argentina ICSID Cases No. ARB/03/17, Order in Response to a Petition for Participation as Amicus Curiae, 17 March 2006. Thus, Amicus practice has accompanied and supported the development of Transparency in investment arbitration, by enabling issues concerning the general public interest to be considered within the arbitral process.


3.7 The new UNCITRAL Rules on Transparency are available not only for UNCITRAL or ad hoc arbitrations, but also for other arbitral proceedings initiated under other rules if they opt into them. Although, there is no general obligation of confidentiality in investment arbitration, there has been a general presumption of respecting the principles of confidentiality and privacy in investment treaty arbitration procedures. UNCITRAL Transparency Rules reverse the general presumption on confidentiality by seeking to establish a balance between protecting confidential business information and national interests on one hand, and openness on the other. UNCITRAL Transparency Rules cover all stages of the arbitration proceedings, including submissions to arbitral tribunals, arbitral awards and the participation of non-disputing third parties such as the already mentioned Amicus Curiae.

e) The EU and its Member States are already increasing transparency

3.8 It is important to underline in this context, that the EU and its Members have already implemented more transparency in their new draft investment treaties with Canada, Singapore and USA.

3.9 The free publication of information and documents submitted in arbitration proceedings has been a well-established practice by some widely well-known free databases, including the List of Pending and Concluded ICSID Cases, the publication of ECT cases and the Permanent Court of Arbitration Repository.

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45 “At the European Court of Justice [...] you have the advocate general, who is there to bring the public interest of the Communities to bear [...] amicus briefs are a substitute for the advocate general” in Thomas Wälde, “Transparency, Amicus Curiae Briefs and Third Party Rights” [2004] OGERL, Vol. 2 Issue 4.


48 Available at: https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=ListCases

49 Available at: http://www.pcacases.com/web/.
The UNCITRAL Transparency Rules reinforce this practice with Articles 2 and 3, where they provide for free publication of all the information submitted in an arbitral procedure, as well as open hearings (Article 6).

3.10 International Investment Arbitration literature has also discussed the possible downside of unrestricted transparency, which fall under four categories: cost, delay, impaired confidentiality and weakened secrecy. The first two elements are closely related as the prolongation of the process typically will be reflected in the financial costs (i.e. the logistics in order to make some information public such as translations and make it available could incur in personnel needed). Publicity also is related to the danger of re-politicization of investment disputes.

f) Conclusion

3.11 Over the past decade, the investment arbitration community and States have continuously sought to implement a wide range of effective tools that supports its legitimacy as a system of investment global governance, where transparency has been a key tool for the accountability of investment arbitration. Transparency has different expressions, with all of them being exercised within the sphere of investment arbitration practice. The new UNCITRAL Transparency Rules have been welcomed by the investment arbitration community since it seeks to strike an appropriate balance between confidentiality and more openness. Indeed, the participation of non-disputing parties, the submission of Amicus Curiae, the expansion of investment arbitration scholarship and free access to many case law databases have played an important role in supporting the argument of investment arbitration as a transparent system. Furthermore, in the TTIP negotiations the EU and its Member States have been actively pushing for more transparency in the investment chapter. The reality is that the system has never been so transparent and the criticism that there is a lack of transparency in ISDS is not supported by the developments and improvements of the past decade.

Criticism 4: Lack of independence and impartiality of arbitrators

4.1 Lack of independence and impartiality in investment arbitration could have severe consequences and certainly might cause legitimate concerns as to the viability of the system. It does not change the fact, however, that such allegations need to be analyzed and reviewed on a case-by-case basis and not as a general objection against investment arbitration. In other words it is up to the parties in

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51 Idem.
the individual dispute to prove their challenges of arbitrators. Therefore, the appropriate question is rather whether the system of investment arbitration includes mechanisms (at the parties’ disposal) envisaging challenge procedure and designed to avoid partiality and prejudice of arbitrators and not whether all arbitrators are biased since they depend on the survival of investment arbitration in its shape nowadays. In fact, a closer analysis proves that impartiality and independence can be (and regularly is) challenged on different levels of investment arbitration system, namely, (i) pursuant to national laws (if applicable), (ii) institutional rules and according to the (iii) IBA Guidelines on Conflicts of Interest in International Arbitration (IBA Guidelines).

4.2 First, one should reflect on the level of national legislation. For illustrative purposes, it has been decided to select the Dutch and Swedish Law, which arguably might be very influential in the investment arbitration context. The choice is not accidental. According to the report prepared by UNCTAD, most arbitrations (but for the ICSID arbitrations) are governed (respectively) by the UNCITRAL International Arbitration Rules (UNCITRAL Rules) and the Arbitration Rules of the Stockholm Chamber of Commerce (SCC Rules). All the UNCITRAL cases considered by the UNCTAD in their statistics were cases administered by the PCA. Presumptively, most of these cases are being held in the Permanent Court of Arbitration (PCA) in The Hague, which means that Dutch law, being the law of the seat, is of relevance. The same applies to the Swedish arbitration law, when the SCC Rules are applicable to the dispute decided in Stockholm. The Dutch Arbitration Act (DAA) that entered into force from 1 January 2015, states in Article 1033 of the DAA that “an arbitrator may be challenged if circumstances exist that give rise to justifiable doubts as to his impartiality or independence.” Moreover, a challenge can, at the request of either party, eventually be brought before the President of the District Court which will decide on the merits of the challenge. The Swedish Arbitration Act (SAA) in section 8 provides a fairly detailed definition of what constitutes impartiality and allows for recourse to the court with regard to the challenge.

4.3 Second, arbitration rules also ensure that in case of an arbitrator’s bias parties may bring an adequate action against a predisposed member of an arbitral tribunal. Indeed, the ICSID Convention explicitly requires that arbitrators “shall be persons of high moral character and recognized competence in the fields of law,

53 Corporate Europe Observatory, Profiting from Injustice suggests: “if an arbitrator’s main source of income and career opportunities depends on the decision of companies to sue, we should wonder how impartial their decisions are”, p. 36.
55 To date, according to the UNCTAD Report, most of the investment cases have been brought before International Centre for Settlement of Investment Disputes (ICSID) and are (usually) governed by its Rules. ICSID, however, is autonomous from national legal orders and, thus, will not be discussed under this paragraph.
56 Book 4, Dutch Code of Civil Procedure.
57 Art. 1035(2) of the Dutch Code of Civil Procedure.
58 The Swedish Arbitration Act, Section 8.
59 The Swedish Arbitration Act Section 10.
commerce, industry or finance, who may be relied upon to exercise independent judgement” and that an arbitrator may be disqualified if he/she manifestly lacks any of the abovementioned qualities. Indeed, in recent ICSID cases (e.g., Caratube v. Kazakhstan (ARB/13/13, Decision on the Proposal for Disqualification of Mr. Bruno Boesch, March 20, 2014); Blue Bank v. Venezuela (ARB/12/20, Decision on the Parties’ Proposals to Disqualify a Majority of the Tribunal, November 12, 2013) and Burlington Resources, Inc. v. Republic of Ecuador (ARB/08/5, Decision on the Proposal for Disqualification of Professor Francisco Orrego Vicuña (December 13, 2013), arbitrators were successfully disqualified. Similarly, the 2010 UNCITRAL Rules provide that “any arbitrator may be challenged if circumstances exist that give rise to justifiable doubts as to the arbitrator’s impartiality or independence.” Finally, the SCC Rules oblige individuals serving as arbitrators to be independent and impartial. Interestingly, a challenge may be made not only in circumstances giving rise to justifiable doubts as to the arbitrator's impartiality or independence, but also if an arbitrator does not possess qualifications agreed by the parties. It should be highlighted that all of these rules not only allow submitting a challenge in case of a doubt, but also require candidates for arbitrators to submit statement of independence confirming their independence and impartiality and pre-emptively monitoring whether the prospective arbitrator may accept its mission or a certain risk of bias exists.

4.4 The third and final point relates to the IBA Guidelines. In a nutshell, the IBA Guidelines comprise two parts: the first one introduces general standards of impartiality, independence and disclosure whereas the second one called “Practical Application of the General Standards” sets out three lists (red, orange and green) of potential conflicts of interests that may occur in arbitration. Application of IBA Guidelines helps to identify the circumstances in which there is a likelihood of conflict of interests. The IBA Guidelines are regularly relied upon in cases of challenges of arbitrators. In addition, conceivably, they gain an additional momentum by being mentioned in the recent (draft) investment treaties such as in CETA.

60 Article 14(1) of the ICSID Convention.
61 Article 57 of the ICSID Convention; the procedure of the disqualification has been further explained in the Rule 9 of the ICSID Rules.
62 Article 12(1) of the 2010 UNCITRAL Rules; the same standard exists in article 10(1) of the 1976 UNCITRAL Rules which also may by occasionally applicable nowadays.
63 Article 14(1) of the SCC Rules: (“Every arbitrator must be impartial and independent.” [emphasis added]).
64 Article 15 of the SCC Rules.
65 See Rule 6 of the ICSID Rules, Article 11 of the 2010 UNCITRAL Rules and Article 9 of the 1976 UNCITRAL Rules, Article 14(2) of the SCC Rules.
Conclusion

4.5 As observed, the system of investment arbitration provides a number of tools which have been created for the sole purpose of ensuring that a lack of independence and impartiality or prejudice of arbitrators can be challenged. While it is acknowledged that investment arbitration has a "public function" and further development of an impartiality and independence standard (for example with regard to the possibility of 'double hats' as counsel or arbitrators) is called for, it does not change the fact that even the contemporary system of investment arbitration is well equipped with mechanisms that can be successfully used in cases of bias. Further, the argument that party-appointed arbitrators are by default predisposed to the position of their appointing party, in the current system is not only incorrect but also overcome by the fact that each party appoints one arbitrator out of three. In turn, it preserves equilibrium during deliberations, even if such an alleged bias can be proven.

It is also necessary to address an argument made in the report of the Corporate Europe Observatory. There, it has been suggested that: “if an arbitrator's main source of income and career opportunities depends on the decision of companies to sue, we should wonder how impartial their decisions are.” It should not be forgotten, however, that the profession of arbitration is an ancient one and it is simply a service of resolving disputes in return for agreed fees. Never had there been any evidence that accepting fees by arbitrators made them biased. Logically, if there had been, international arbitration would have never been used as frequent as it is. Therefore, the implication that collecting remuneration (fees) for the contract of service (resolving disputes) makes the service-provider (an arbitrator) predisposed is one bridge too far to say the least.

The system of investment arbitration includes effective mechanisms that can be used against an alleged bias. These tools include actions for challenge before national courts and within the arbitral institutions. The arbitration community took a bottom-up initiative to improve the standard of impartiality and independence applicable to the arbitrators (see IBA Guidelines). While "new" and "better" standards can still be developed, the investment arbitration system in its current form ensures that arbitrators are impartial and independent.

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68 Corporate Europe Observatory, Profiting from Injustice p.36.
Criticism 5: The elite group of arbitrators

5.1 Corporate Europe Observatory identified 15 individuals, which it called "an elite 15" and claimed that "15 arbitrators have captured the decision making in 55% of the total investment treaty cases known today." What the report fails to properly address, however, is the underlying principle of international arbitration, namely the principle of party autonomy. In the system of international arbitration, parties are free to structure the procedure as they wish, but also, most importantly, to select and appoint an arbitrator of their own choice. This freedom of selecting the arbitrator applies to both the claimant – the investor – and to the respondent – the State.

5.2 As a consequence, the fact that some arbitrators are more often selected than others is a result of party choice. Even the Corporate Europe Observatory highlights that "the elite 15" "have been repeatedly ranked as top arbitrators by well-known surveys". It only proves that these individuals are at top of their professions and, as such, it does not come as a surprise that, where the stakes are high, parties to the proceedings (thus both the investor and the State) prefer to have seasoned arbitrators at the panel. The Corporate Europe Observatory table with "a few biographic details you might not find in the industry's own rankings" shows exactly that this "elite 15" is a highly experienced group of arbitrators. In fact, it lists individuals that were judges of the international courts and tribunals, people with experience in policy making and former diplomats; individuals who are more than capable of dealing with complex disputes of public law character and have broad experience that is not restricted to commercial law disputes.

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69 Corporate Europe Observatory, Profiting from Injustice p.38. What the report fails to highlight is that the cases were decided by three members tribunals, nor does it provide details on the outcome of these cases.
70 If parties fail to create an appropriate appointing tool, the institutional rules will provide for the fall-back mechanism in case of parties' default. Since most of the investment arbitration cases are governed by the ICSID Convention/Rules and the UNCITRAL Rules, the relevant default rules in these texts are that either each party appoints its arbitrator and the parties will also jointly agree to the appointment of the presiding arbitrator (see Rule 3 of the ICISD Rules in connection with the ICSID Convention Article 37(2)(b), if the tribunal is not constituted within 90 days see Rule 4 of the ICSID Rules) or that each party appoints its arbitrator and party-appointed arbitrators choose the presiding arbitrator (see Article 7(1) of the 1976 UNCITRAL Rules and Article 9(1) of the 2010 UNCITRAL Rules. If the party appointed arbitrators do not agree on the choice of the presiding arbitrator within 30 days of the appointment of the second arbitrator, see Article 7(3) of the 1976 UNCITRAL Rules and Article 9(3) of the 2010 UNCITRAL Rules.
71 Corporate Europe Observatory, Profiting from Injustice, p.38.
72 Ibid., pp.38-41.
73 Hon. Charles Brower has served as a judge of the Iran-U.S. Claims Tribunal, ad hoc judge of the Inter-American Court of Human Rights and since 2014 he serves as an ad hoc judge at the International Court of Justice. Marc Lalonde was an ad hoc judge at the International Court of Justice. Judge Stephen M. Schwebel was a judge of the International Court of Justice, also acting as The ICJ President.
74 Marc Lalonde served i.a. as a Minister of National Health and Welfare, Minister of Justice, Minister of Finance; Daniel Price.
75 L. Yves Fortier; Francisco Orrego Vicuña.
Moreover, the Corporate Europe Observatory Report shows the "frequency of elite arbitrators sitting side-by-side as co-arbitrators" inclining, as the title of the section suggests, to "keep investment arbitration cases in the family". Again, it must be stressed that parties appoint arbitrators (but for a presiding arbitrator). Therefore "elite arbitrators" can (generally) sit together in one panel only when: (i) parties appointed them, (ii) one of them was appointed and the second one is a presiding arbitrator. Presiding arbitrators will be selected (i) upon agreement of the parties, (ii) joint decision of party appointed arbitrators (thus indirectly by the parties) or eventually by the appointing authority (such as ICSID, the SCC or the PCA). It is therefore incorrect to present these 15 arbitrators as a clique that has the decisive vote on how a composition of a tribunal in a random case is formed since it is only the parties to the dispute that have a vote in the selection procedure. It should also be noted that the mere fact of sitting in the same panel proves nothing as to the outcome of the case decided.

Additionally, even if one wants to argue that the system of investment arbitration provides incentives for the prospective pool of arbitrators to use the popular adage don't bite the hand that feeds you, it should also be noted that the system provides an incentive also for profiled individuals who share the viewpoints of and are sympathetic towards States. For example, the Corporate Europe Observatory Report itself describes Brigitte Stern as the "State's favourite choice as arbitrator". Indeed, recently she has been challenged in several cases for her repeat appointments by States (e.g. CEAC Holdings Limited v. Montenegro, ARB/14/8 and Highbury International AVV, Compañía Minera de Bajo Caroní AVV and Ramstein Trading Inc v. Venezuela, ARB/11/1).

As highlighted earlier, parties are free to choose their appointees to the arbitral panel. It is logical that they will select persons they expect to be more sensitive to their positions. Consequently, if one concludes that "pro-investor" arbitrators profit from the system, one must similarly conclude that also "pro-state" arbitrators exist and also gain from the investment system. Be that as it may,

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76 Corporate Europe Observatory, Profiting from Injustice, p.42.
77 For appointment of arbitrators under ICSID, see fn. 70.
78 For arbitral appointment under UNCITRAL Rules, see fn. 70.
79 Corporate Europe Observatory, Profiting from Injustice p.36 states that: "Given the one-sided nature of the system, where only investors can sue and only states are sued, a pro-business outlook could be interpreted as a strategic choice for an ambitious investment lawyer keen to make a lucrative living." As long as such an interpretation can be feasible with regards to lawyers acting as counsels it will not hold true with regards to arbitrators.
80 Asymmetry in the system (i.e. that only investors can sue the states) does not change anything from the perspective of an arbitrator. As long as there is a case against a state, such a state will need to appoint an arbitrator and it will seek a person understanding of its position. Therefore, prospectively, an arbitrator "favoring" the position of the investor and an arbitrator "favoring" the position of the state will be selected. It should also be noted that the asymmetrical system is not new in international adjudication. By way of example, a human rights claim before the European Court of Human Rights can be also brought only against States. In both cases the rationale for the asymmetry is the legal position of the individual/investor vis-à-vis State. For further reading see Rogers, Catherine A., “The Politics of International Investment Arbitrators” [2013] 12 Santa Clara Int’l L. Rev, Penn State Law Research Paper No. 52-2013, pp.252-253. Available at SSRN: http://ssrn.com/abstract=2347843 [last accessed 30 October 2014].
since States and investors can select the arbitrators of their choice, the parties are able to maintain the balance of interests within the tribunal.  

Moreover, if States are not satisfied with the current system of appointments of arbitrators, they are able to change it. For example, the roster system as introduced in CETA may have an influence in changing the dynamics of the selection procedure. According to the new CETA system, if the party-appointed arbitrators fail to agree on appointing the chair, the chair will be appointed by the Secretary General of ICSID based on a list, which was pre-determined by the CETA contracting parties. The fact that the roster will be compiled exclusively by the CETA contracting parties will allow them to select "pro-state" arbitrators for the roster. This will tilt the balance within the arbitral tribunal to their advantage, because the Respondent state can potentially select 2 of the 3 arbitrators, namely, its own arbitrator and the chair from the roster, if no chair has been appointed by the arbitrators. This may undermine the very foundations of arbitration (and of justice): the equality of arms between the parties.

Similarly, the proposal of the European Commission for a permanent investment court will allow States to select all the judges of this court exclusively, thereby excluding any arbitrator they consider to be "pro-investor". At the same time, the investors will not be able any more to chose an arbitrator of their choice. Thus, there is already a trend visible towards enabling States to exclusively select the arbitrators/judges, while at the same time excluding the involvement of the investors/claimants.

**Conclusion**

5.5. To conclude, it should be noted that investment arbitration is based on a system of party autonomy in which designating parties appoint their own arbitrators. In doing so both parties choose individuals they believe are likely to be sympathetic to their cause. If States indeed feel so uncomfortable with the current pool of arbitrators, they are totally free to expand that pool by selecting "new" individuals. In this way States can also actively widen and improve the composition of the pool by selecting more women and more non-Western individuals.

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81 Again, it is necessary to stress that having a better understanding of the position of an investor or a state does not amount to prejudice of arbitrators and it does not affect arbitrators’ obligation to remain independent and impartial.

Criticism 6: Costs: diversion of public money from public goods and services

6.1 The growing number of ISDS cases and the broad range of policy issues they raise have put the system of investment arbitration under intensive scrutiny by States, NGOs, and other stakeholders. This discontent is the result of a perceived failure in the functioning of the ISDS system, particularly, in relation to (i) its legitimacy and transparency (ii) problems of consistency of the arbitral decisions (iii) concerns about the independence and impartiality of arbitrators and (iv) the alleged costly and time-consuming nature of arbitrations.

6.2 This section seeks to provide some clarity regarding the alleged high costs of investment arbitration. We will also analyse empirical evidence to determine whether domestic courts are the most suitable institutions to hear investment complaints lodged against host states.

6.3 FDI is positively correlated with the quality of domestic legal institutions. In a recent study by the International Monetary Fund in relation to the Italian judicial system, it was found that "the inefficiency of the Italian judicial system has contributed to reduced investments, slow growth, and a difficult business environment." Therefore, the reduction of FDI as a result of inefficient domestic courts should be taken into account when evaluating the relative costs of ISDS.

6.4 Notwithstanding the high costs associated with international arbitration, businesses often still prefer ISDS as a mode of dispute resolution over litigation in many domestic courts, because it is less time-consuming, more effective and, as a result, often less expensive. National courts, as an alternative to ISDS, do not necessarily inspire greater confidence.

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83 In some instances, States have denounced the ICSID Convention while others have withdrawn from the ICSID Convention and withdrawn or renegotiated their own treaties. For example, Bolivia withdrew from ICSID in 2007 and was followed by Ecuador in 2009 and Venezuela in 2012. In 2012, Argentina announced that it would withdraw from ICSID although it is still ICSID member, whereas at the same time Canada has recently ratified the ICSID convention.

84 UNCTAD, Investor-State Dispute Settlement [2014] Series on Issues in International Investment Agreements II.


87 OECD, Investor-State Dispute Settlement, Public Consultation: 16 May – 9 July 2012, at p. 18. The OECD has surveyed publicly-available information about ISDS costs. The survey showed that legal and arbitration costs for the parties in ISDS cases averaged over USD 8 million.

Despite the largest cost component identified in ISDS cases relating to the fees and expenses incurred for each party's legal counsel, there is no comprehensive study that shows that litigation in all domestic courts is less costly or that States need to allocate fewer resources within their own jurisdictions. Indeed, the actual costs of the domestic court system are difficult to measure because they are "hidden" and covered by the national budget, i.e., the various costs are "generalized" and covered by the whole population. Furthermore, within the framework of the ISDS system, States are free to choose their own legal representative: either external or in-house.

The IIA universe consists of more than 3,200 agreements, made up of 2,902 BITs and 334 "other IIAs" (such as free trade agreements or economic partnership agreements with investment provisions). Yet only 568 treaty-based cases have been reported, in which 98 States have acted as respondents. This must be compared to the thousands (or tens of thousands) of claims that domestic courts must deal with on an annual basis, and the tens of millions of euros required by States to establish an independent judiciary. In-house lawyers, everyday expenses of running national courts, staff, etc. all come at a cost.

Looking at the established nations in the EU and the US, even here the judicial systems in the EU and US are very diverse and vary from state-to-state. The quality of judicial independence and impartiality differs from EU Member State-to-EU Member State. The single market in judicial framework does not exist and will not exist in the foreseeable future in the EU. Indeed, the 2015 EU Justice Monitor confirms again the huge divergences in the quality of the judicial system in the various EU Member States. Similarly, the quality and expertise of judiciary also differ from state-to-state in the U.S. One of the most important considerations to ensure that foreign investors consider all EU member states and all U.S. states equally attractive is to provide the same high standard of protection across these regions. Otherwise, more developed Member States and US states with more developed judicial systems will attract greater investment and the gap will only increase.

Finally, one should also note that to date there are nine BITs in force between EU Member States and the US. This means that as the system currently stands, US investments are protected in those Member States by treaties being denounced by critics as "poor". The EU is now in a position to rectify the current treaties and create solidarity and equal treatment amongst the Member States and their investors by concluding a deal with ISDS covering all EU Member States.

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89 See fn. 87. Legal counsel and experts' fees are estimated to average 82% of the total costs of a case. Arbitrators fees average about 16% of costs and institutional costs amount to 2% of the total.


Conclusion

6.9 While the public debate continues to gain momentum, weighing the pros and cons of ISDS and its (real) alternatives deserves careful attention. As the domestic judicial systems do not seem to be better equipped for the resolution of investment arbitration disputes, ISDS offers a more suitable mechanism to deal with this task. The alleged high costs for such a private justice procedure are limited to those incurring mostly for each party’s legal counsel. On the other hand, it is clear that foreign investors often feel not comfortable to bring a claim against the host State before its domestic courts. Indeed, studies confirm that many judicial systems are not meeting the minimum standards of the Rule of Law and are slow and inefficient. Therefore, international arbitration is a necessary and useful alternative for resolving international disputes. Despite the high costs for international arbitration and the low chances of ultimately receiving compensation, foreign investors still prefer international arbitration instead of domestic courts. At the same, it should be noted that there is no comprehensive study proving that domestic litigation is more effective and/or less costly than ISDS.

Criticism 7: "Chilling effect" on state regulatory powers

a) Introduction

7.1 For a useful discussion of the regulatory chill theory, it is first of all necessary to narrow it down from a mere logic to a workable definition. In their study for the Netherlands Ministry of Foreign Affairs, Professor Tietje and Associate-Professor Baetens extensively touch on the issue of regulatory chill. They define regulatory chill as the situation in which ‘a State actor will fail to enact or enforce bona fide regulatory measures because of a perceived or actual threat of investment arbitration’ in which they distinguish between a) not drafting particular legislation in anticipation of arbitration, b) chilling legislation upon awareness of arbitration risks, and c) chilling legislation after the outcome of a specific dispute. The definition rightfully assumes that one agrees that the chilling of male fide regulatory measures via ISDS does not merit any discussion, although there are voices favoring the exclusion of ISDS in any BIT as ‘local citizens and companies do not have this option either’.

92 Ibid.
93 Prof. Dr. Tietje and Associate Prof. Dr. Baetens and Ecorys Rotterdam, "The Impact of Investor-State-Discpute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership" [2014] Study prepared for the Minister of Foreign Trade and Development Cooperation, Ministry of Foreign affairs, The Netherlands, para. 68.
7.2 The regulatory chill theory appears to presuppose that ISDS impacts on legislative processes. However, as Tietje and Baetens show, of all concluded ICSID cases up to 2014, 47% relate to executive or administrative acts, such as permits and licenses, whereas only 9%, or 14 cases, relate to legislative acts. Citing researchers Jeremy Caddel and Nathan Jensen, they note that 'given the low rate of disputes involving legislative branch activity, arguments that investor-state arbitration may encroach on the legitimate prerogatives of domestic governments appear to be overstated. Democratic legislatures should embrace investor-state arbitration as an additional check on executive branch misbehavior'.

7.3 Imagine that a government concludes that oil and gas production ought to be state-controlled. It believes this should enhance the government’s international geopolitical standing, while domestic price control would shield the population from international oil prices fluctuations. The government therefore decides to expropriate half the ownership of a large foreign-owned gas production facility without paying just compensation. It also enacts laws that empower the government to set the consumer gas prices independently whilst restricting gas exports. This government and its parliament believe that the government action serves the public interests. However, the compensation of the investor in these cases is also an important parameter. In this context, should these regulations be "chilled" to a level that respects property rights? If so, would the local judiciary necessarily strike down the public policy choices made by the legislative and executive branches of government? Practice in countries like Argentina or Venezuela suggests that the judiciary of a country taking such radical decisions may not be able or willing to counter the will of its government. This is precisely why BITs contain provision for ISDS. The contracting states permanently offer foreign investors their agreement to engage with an independent, non-political forum for dispute settlement in instances where a foreign investor feels its investment is treated discriminatorily or expropriated without just compensation and informal dispute resolution no longer seems fruitful.

7.4 Although in many ISDS-cases the problem is not this straight-forward, it is useful to bear in mind the basic rationale behind international arbitration as a solution to investor-state disputes. Foreign investors do not lightly decide to request international arbitration. It is expensive with no guarantee of success, and although it may resolve the legal and financial aspects of a dispute, the relationship with the host state will not necessarily be restored through the process. Countries that seek to align their laws and regulations regarding e.g. employment or environmental protection, with international standards pertaining to these policy fields are not likely to be successfully challenged by

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95 J. Caddel and N. Jensen, “Which Host Country Government Actors are Most Involved in Disputes with Foreign Investors?” [2014] Columbia FDI Perspectives: Perspectives on topical foreign direct investment issues by the Vale Columbia Center on Sustainable International Investment No. 120 http://academiccommons.columbia.edu/catalog/ac:173529, in: Tietje and Baetens, see fn. 93.
foreign investors via ISDS. So, from where do the allegations of "regulatory chill" derive?

b) **The accessible logic of the regulatory chill theory**

7.5 If you were to face significant liabilities if you took a particular action, you are less likely to take that action. That is in essence the rationale behind the ‘regulatory chill’ argument against ISDS. In a democracy, policy making and enacting regulation centers around finding a balance between all interests involved in a way that enjoys the majority support in the legislative branch. Consequently, there can be a minority or minorities – business, labor unions, academic experts or non-governmental groups – that would like to see a different balance being struck in a specific instance. For example, a government can decide to re-allow nuclear power activities, leading environmental groups to argue that energy-related and environmental legislation has been ‘chilled’ in favor of economic interests.

7.6 If a legal act has been enacted without due process or if it defies the rule of law, for example because of its discriminatory nature or its inconsistency with overarching legal principles, the act, its implementation or enforcement could be ‘chilled’ by the judiciary branch on the basis of a lawsuit filed by an interested party. Indeed, chilling regulation is at the core of policy and law making by the legislative and executive branch and it depends on where one stands in a specific discussion whether the (perceived) chill provokes a good or unwanted outcome. But, of all influences on the regulatory process of a host state, does ISDS have an inappropriately chilling effect? Does it unduly restrict states’ regulatory powers?

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96 Avoiding disputes between states and investors by providing clarity to investors on internationally recognized standards relating to various public policy areas is one of the ways in which the OECD Declaration on International Investment seeks to promote international investment. These standards, in the form of recommendations to investors pertaining to *inter alia* corporate governance, human rights, employment, environment, anti-bribery and taxation, are set at OECD, ILO or UN level by governments in cooperation with business and trade unions. Although recognizing foreign investors’ right to seek arbitration, these recommendations embodied in the OECD Guidelines for Multinational Enterprises, annex to the said OECD Declaration, also serve as an implicit indication of what standards should not be challenged by investors. More information on the OECD’s work on investment can be found on [www.oecd.org/investment/](http://www.oecd.org/investment/). See also the *Chemtura v. Canada* case where the existence of a governmental decision taken for a public purpose renders the standard for challenging the regulatory decision very high. *Chemtura Corporation (Formerly Crompton Corporation) v. Government of Canada* [2012] NAFTA ch.11, Award.

97 An interesting example can be found in the prejudicial questions that have been asked by administrative courts in Austria and the Netherlands respectively in relation to the interpretation and implementation by the governments of these two countries of the 2009 EU Emissions Trading System Directive. For the decision of the Dutch court (Uitspraak 201311081/1/A4, 11 June 2014) see: [http://www.raadvanstate.nl/uitspraken/zoeken-in-uitspraken/tekst-uitspraak.html?id=79518](http://www.raadvanstate.nl/uitspraken/zoeken-in-uitspraken/tekst-uitspraak.html?id=79518). In the Dutch case, the claimants allege that the Netherlands has wrongfully interpreted the scope of the aforementioned EU Directive in a narrow manner, which led to less emission rights than claimants allege they are entitled to. Indeed, business interests were allegedly ‘chilled’ in favour of reducing Dutch emissions.
c) Can regulatory chill be measured?

Measuring the aforementioned categories of chill that result from ISDS is virtually impossible as it is impossible to find out which draft legislation has been withheld or whether ISDS-risks, more than e.g. risks to domestic legal procedures by nationals, constituted the determining factor in chilling proposed legislation. As Tietje and Baetens rightfully note, 'regulations related to public interests such as the environment, health and natural resources are often fraught with political debate, and the possibility of ISDS may be just one of a number of factors leading to the regulatory chill'.

The disputes most commonly mentioned as causes of regulatory chill are still pending and have not led to actual changes in legislation. In fact, after Australia also France and New Zealand are now considering following Australia in introducing mandatory plain packaging of cigarettes. It seems hard to imagine that these countries presented such legislation without being aware of the similar laws Australia enacted and the challenges it faces upon that enactment.

Arbitral awards do not call upon, let alone force, host states to chill their laws and regulations; they only deal with the question of the right to compensation under the given circumstances on the basis of the relevant BIT. The government’s persuasion to roll back specific legislation may come from the substantial motivation laid down in the award, leading to a government's reconsideration of which other measures can equally lead to its policy ends while observing its international law obligations.

Even where a state has indicated that the apparent risk of ISDS or the outcome of a particular case forms a risk to its regulatory powers, such a statement could be made for political reasons. The recent termination of BITs by Indonesia and South-Africa for example may indeed serve to protect these countries’ regulatory powers, however not necessarily with the aim to protect public interests such as human rights or the environment. Protectionist motives could also play an important role in a government’s position vis-à-vis investor protection and ISDS, which seek to eliminate discriminatory treatment.

In short, a wide array of factors lead to particular laws being enacted and other options to be left aside whereby the compromise of relevant interests that is made with each law or policy implies that all government action is chilled vis-à-vis certain interests. It is impossible to measure the influence of ISDS as a potential factor on law and policy making processes, although ISDS is not likely to have more influence on these processes than e.g. the legal actions domestic stakeholders can initiate within the local legal system.

98 See fn. 93, para. 72.
99 See Philip Morris Asia Limited v. The Commonwealth of Australia; Lone Pine Resources v. Canada. All available on the ICSID web list of cases.
100 See for example the Financial Times of 25 September, 2014: "France to adopt plain tobacco packaging and restrict e-cigarettes" Available at: http://www.ft.com/intl/cms/s/0/06f8731c-44bf-11e4-bce8-00144feabdc0.html#axzz3FLl05ElL.
d) Conclusion

7.11 Law and policies are enacted within the boundaries of general principles of law, such as due process and human rights, and of policy principles, such as proportionality and subsidiarity. Where such boundaries are crossed, legislative or executive acts can be chilled by various mechanisms, such as parliamentary debate, the local judiciary or ISDS. However, describing ISDS as a force that unduly restricts countries’ legislative branch in exercising its sovereign powers to regulate or that unduly chills existing or proposed legislation has no basis in political science or analysis of international (investment) law and ISDS statistics. The fact that regulatory chill cannot be measured may help those who support the theory when influencing public opinion. However, in the scholarly or policy debate, this impossibility should nullify the regulatory chill theory, as does the fact that the vast majority of ISDS-cases are not brought on the basis of legislative acts, but rather due to executive acts. Although often cited cases in this respect, such as those concerning Phillip Morris and Vattenfall, may stem from legislative acts, the fact that thus far these acts have not been ‘chilled’ – let alone unduly chilled – further invalidates the regulatory chill claim.

Criticism 8: ISDS allows international companies to bypass national judicial systems

8.1 One of the main arguments against the inclusion of an ISDS provision in the TTIP is that this mechanism allows foreign companies to bypass national judicial systems, possibly at the expense of domestic investors. Therefore, the critics argue that this kind of provision would grant foreign investors greater procedural rights than domestic investors who do not have access to this parallel, extrajudicial legal track. Moreover, the EU and US have well-functioning domestic legal systems and provide for robust protection of property rights. Thus, the critics ask: What is the need for international arbitral procedures when investors have access to such trustworthy domestic judicial systems101?

However, the IIA system does not seek to by-pass domestic courts, but to complement them by granting investors an additional effective forum:

- In fact, a number of IIAs oblige investors to pursue (or even to exhaust) local remedies before referring the dispute to international arbitration. For example, the BIT between China and the Ivory Coast prescribes that the investor “shall have exhausted the domestic administrative review procedure […], before submission of the dispute to the aforementioned arbitration procedure”.

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101 The European Commission’s overview of European judicial systems reveals that 14 member states have a judicial independence ranking under 50, and 4 under 100; The 2014 EU Justice scoreboard, figure 29, available at http://ec.europa.eu/justice/effective-justice/files/justice_scoreboard_2014_en.pdf.
• In a recent award, the tribunal in *Dede v. Romania* dismissed all the investor’s claims and concluded that it lacked jurisdiction in relation to the matter before it because the investor had not satisfied the jurisdictional requirement in the Romania-Turkey BIT (1996). Under this BIT, the investor’s right to submit the dispute to arbitration is subject to, either, the local litigation being unfinished within one year or the exhaustion of local remedies.¹⁰²

• Investors are often not able to submit a claim before domestic courts on alleged violations of an IIA. To date, investors’ claims before national tribunals have been based solely on domestic law and not international law.¹⁰³ For example, investors are precluded from submitting NAFTA-based claims in the domestic courts of Canada and the United States.¹⁰⁴

• Finally, it may be difficult in some countries to ensure that the rule of law is applied by domestic courts or their executive branches in an impartial and independent way which results in a final decision consistent with fundamental principles of public law. One example where this was an issue was in the case of *Transglobal Green Energy v. Panama*. In this case, the investor had to resort to international arbitration because the Panama Government failed to implement the decision of Panama’s Supreme Court and, thereby, breached the Panama-United States BIT.¹⁰⁵ Another example is the recent *Yukos* case, which showed that it was factually impossible for the Yukos shareholders to resort to domestic courts due to their lack of independence¹⁰⁶.

8.2 Article 26 of the ICSID Convention allows States to make exhaustion of domestic remedies a condition of consent to arbitration. However, relatively few States have included such a requirement in their investment treaties. On the contrary, over the years, developed countries have sought to grant their investors direct access to international arbitration; almost no modern BIT contains a full exhaustion clause.

8.3 The preference for international arbitration for investors involved in a dispute against the host state based on an international investment treaty is understandable since investors seek a neutral forum to resolve their disputes. With this understanding, investment arbitration should not be seen as simply the viable route in the face of ‘untrustworthy’ domestic courts, but rather the most viable option in light of the international character of the dispute.

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¹⁰² Ömer Dede and Serdar Elhuseyni v. Romania [2013] ICSID Case No. ARB/10/22, Award, paras. 219 and 254.
¹⁰³ See fn. 80.
¹⁰⁴ See, for the United States, the *North American Free Trade Agreement Implementation Act*, Pub. L. 103-82, sec 102(c) and, for Canada, the *North American Free Trade Agreement Implementation Act*, SC 1993, c 44, sec 6(2).
8.4 Another option for foreign investors is the practice of espousal of claims in the framework of diplomatic protection offered by the States. However, this option has been regarded as arbitrary and unsatisfactory for investors. This is because the investor's home State has complete discretion over the commencement, prosecution and settlement of such a claim as well as whether the investor will in the end obtain full compensation, even if the State received it. Moreover, litigation in domestic courts of States other than the host State is liable to lead to State immunity and territorial jurisdiction problems; hardly a promising alternative.

8.5 Going a step further, by removing the requirement of exhaustion of domestic remedies and allowing immediate access to international procedures, BITs guarantee faster and more efficient proceedings. Although the average BIT arbitration nowadays also takes three years, this is still considerably faster than the time it takes to exhaust available remedies in many developed national judicial systems.

8.6 In general, domestic courts of the EU member states do provide reliable mechanisms of resolving disputes. However, the quality (assessed from the effectiveness, efficiency and accessibility standpoints) of domestic judicial systems differs from one state to another. A notable example of inefficiency of domestic dispute resolution system is the use of the "Italian torpedoes". In essence, "Italian torpedo" is an abuse of the lis pendens rule. The rule is set forth in Brussels I Regulation and embodies a formal criterion to avoid parallel proceedings: if another court is already seized of a matter, the second court seized must decline jurisdiction. Although the very purpose of this jurisdictional criterion is to ensure predictable, certain and neutral litigation outcomes, it has been used strategically to delay the proceedings by instituting a legal action in Italy regardless of whether or not Italian courts have jurisdiction, taking

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107 Under this public law notion, governments take over an investment claim of their nationals against another State after they have exhausted all local remedies, make it their own claim and then proceed to litigate it on a State-to-State basis, see Christoph Schreuer “The relevance of Public International Law in International Commercial Arbitration: Investment Disputes” [2006] available at www.univie.ac.at/intlaw/pdf/csunpubpaper_1.pdf
advantage of significant delays characterizing Italian courts. Shortcomings of domestic judicial systems have been identified also in the US. For example, NAFTA tribunal in Loewen v. US, reviewing the Mississippi trial, characterized it as “a disgrace” “[b]y any standard of measurement.”

8.7 There are good reasons for granting foreign investors access to international arbitration. Investment treaties increase the flow of FDI and legal certainty for foreign investors is crucial. States are aware of this and therefore have concluded thousands of IIAs, which include provisions for the national treatment of foreign investors in order to safeguard equal treatment of national and foreign ones and to secure that States will conform to internationally set minimum standards of treatment. Moreover, it can not be denied that foreign investors are always less familiar with local laws and court practices. It is also a fact of life that domestic courts are perceived by foreigners to favour local parties. This perception is particularly strong, if a foreign investor brings a claim against a local or national government.

Conclusion

8.8 International arbitration is the most efficient way to handle international investment disputes as both diplomatic protection and domestic court litigation fail to offer a realistic alternative. International arbitration offers an objective and independent international judicial procedure on the basis of internationally accepted standards that grants direct access to the investor without having to depend on its State of origin. Furthermore, it is the most appropriate forum in light of the international character of the dispute providing the investor with a neutral forum to settle its dispute.

113 Loewen Group Inc. and Raymond L. Loewen v. United States of America, ICSID Case No. ARB(AF)/98/3, Award, 26 June 2003, para. 119. In this case, Canadian investor Loewen sought to appeal the $500 million verdict and judgment of a Mississippi court rendered against it but was confronted with the application of an appellate bond requirement. Mississippi law requires an appeal bond for 125% of the judgment as a condition of staying execution on the judgment but allows the bond to be reduced or dispensed with for “good cause”. In spite of the investor’s “claim that there was good cause to reduce the appeal bond, both the trial court and the Mississippi Supreme Court refused to reduce the appeal bond at all and required Loewen to post a $625 million bond within seven days in order to pursue its appeal without facing immediate execution of the judgment. According to Claimants, that decision effectively foreclosed Loewen’s appeal rights.” Id., para. 6.
114 A national treatment provision requires the host state to afford equivalent treatment to foreign investors as it does to entities which are nationals of the host state.
115 See Article 14 (1) of the ICSID Convention and Art 11 of the UNCITRAL Rules.
Criticism 9: Both the US and the EU have efficient Rule of law legal systems. There is no evidence that investors have ever lacked appropriate legal protection through these systems.

a) Introduction

9.1 In addition to confirming recourse to domestic courts, IIAs generally include ISDS through international arbitration as a way to resolve issues at a non-politicized, neutral platform. National courts may also be reluctant to enforce or take into account international agreements and obligations, as has been argued in the case of the United States. The opposite idea has also been pushed as an argument why ISDS would be redundant: If both signatories to a bilateral investment treaty have a clear separation of powers and have strongly established the rule of law in their domestic legal systems, one no longer needs an international arbitration clause. Is there validity to these views and how do they apply to the practice of the EU and the US and their negotiating of the TTIP?

b) Examining the added value of ISDS to legal protection

9.2 One can think of several ways of determining whether ISDS is necessary given the rule of law situation of a particular country. Non-governmental organizations (NGOs) have conducted analyses of countries’ performance on securing the rule of law, such as US-based World Justice Project. This NGO uses 47 indicators for its analyses, divided over nine themes: constraints on government powers; absence of corruption; open government; fundamental rights; order and security; regulatory enforcement; civil justice; criminal justice; and informal justice. As for the rule of law implementation by EU Member States specifically, one could also look at the case law of the European Court of Human Rights. Here, one will find numerous confirmed claims, also concerning the protection of property, against EU Member States with generally advanced solid legal systems. A third approach would be to look at the number of arbitration cases that have been filed against governments from, in this case, EU Member States and the US, especially where these have led to a settlement or an award in favor of the investor.

c) The relevance of individual countries’ rule of law performance in international law

9.3 International investment law, whether of a substantial or procedural nature, is part of public international law and concerns international state and non-state actors. From this perspective, it is self-evident that when a state agrees to abide by a set of rules, their enforcement or compensation claims relating to the non-

116 http://worldjusticeproject.org/
117 See for example Hutten-Czapska v. Poland (ECHR, application no. 35014/97).
observance of those rules is also dealt with internationally, or, that those actors who rely on these agreements have the option to seek their enforcement internationally. This can be done by an international court or through international arbitration on an ad-hoc basis.\(^{118}\) Whether a state party to a particular international agreement has an effective national legal system that could deal with claims from foreign actors independent from the executive and legislative branches is therefore irrelevant. After all, a foreign investor demanding compensation following the expropriation of his property via an international arbitral tribunal does not challenge the host government act as such, but alleges that the host government has failed to act in accordance with its international law obligations and is therefore entitled to compensation.\(^{119}\) At the same time, countries that enact laws and regulations with due process and that respect the rule of law have nothing to fear from international arbitration as their acts are not likely to be challenged. It is for this reason that States such as the Netherlands and the UK have - after more than 50 years of investment treaty practice - never been challenged by foreign investors. Also, it is only after more than 50 years that Germany, France and Switzerland face their first claims.

9.4 From a strict international law perspective, an individual country's domestic rule of law performance is less relevant when discussing enforcement mechanisms of international legal obligations. The same holds true for arguments stressing the need for ISDS in treaties with countries where local courts are seen as reluctant to enforce these international agreements when deciding on acts of the national or regional government. The latter may indeed very well be the case in practice, and therefore on itself merits inclusion in the overall reasoning on the need to include ISDS. However, in the discussion on the architecture of international law, it should be clear that serious international law commitments come with serious international enforcement options. If the latter are absent, commitments risk becoming mere political statements and, in the case of IIAs, are not likely to promote foreign investment beyond existing levels.

d) Conclusion

9.5 It is self-evident that international obligations that states have entered into also need to be enforceable in an international setting, be that via a permanent or an ad-hoc dispute settlement body. The fact that international arbitration clauses are so common in IIAs is the practical reflection of this argument of legal theory.\(^{120}\) Now that the EU and the US are willing to address current criticism on

\(^{118}\) Indeed, an international court for investment claims does not exist, although the idea is now pushed by the European Commission.

\(^{119}\) See for example ExxonMobil’s press statement following its award against Venezuela, in which it recognizes the host country’s right to nationalize its property upon payment of fair compensation. See for example the Financial Times’ coverage of the case: http://www.ft.com/intl/cms/s/0/d790a6f2-5004-11e4-a0a4-00144feab7de.html#axzz3HfEzfQ16

elements of investment protection, amongst which the standards of treatment and ISDS, demanding that ISDS should be left out in TTIP’s investment chapter would be a missed opportunity for everyone to shape a balanced global standard for investment protection and modes of its enforcement.

9.6 Moreover, the EU has frequently stressed that TTIP would serve as an example for its future international investment agreements. If this is the case, an international arbitration clause cannot be left out of the deal, as both the EU and the US have already publicly acknowledged. Leaving it out here will make it much harder to argue that the clause is needed in IIAs with other countries. In that case, fewer IIAs will be concluded and the benefits of a more open international investment climate will not be reaped.

**Criticism 10:** When governments concede to demands for ISDS provisions, they may be less willing to agree to other reforms, such as greater market access

10.1 Opening up one’s market to foreign investments with non-discrimination guarantees is quite a big step after merely liberalising trade in the greater scheme of international economic integration. Whilst domestic producers in critical sectors could still be protected via import tariffs, such protection is much harder when sectors are faced with foreign investors in their own market. If a government has to ensure non-discrimination, due process and other internationally recognised standards of treatment of aliens vis-à-vis foreign investors it may feel inclined to exclude particular domestic industries, such as energy supply and critical infrastructure. Supposedly, this is even more so the case when offering international arbitration, ISDS, to foreign investors when they feel their rights are not upheld. Is there any truth in this assumption?

10.2 The extent to which market access will be granted, how investors’ rights are defined and what courses for redress are offered will be the result of negotiations between the parties to an international investment agreement. This can either be a BIT or a FTA that also covers FDI. Obviously, given their broad remit, the number of potential hurdles and bargaining chips in FTA negotiations is much larger compared to when negotiating a BIT. From the outside it may prove very hard to reverse-engineer the bargains made during the negotiations. Whether the inclusion of ISDS or the limitation of market access came first may then seem like a chicken or egg story: has market access been limited because ISDS was included, or was ISDS accepted because market access already was limited for other policy reasons?

10.3 An important pre-determinant is whether one starts from a post-establishment or already made investments-only basis or a pre- and post-establishment basis,
which also includes market access. The standards of treatment of foreign investors under European BITs mostly apply to post-establishment investments only. However, the new EU FTAs that include an investment chapter also deal with the liberalisation of trade in services. Those provisions can be relied upon in relation to pre-investment activities, only without the ISDS guarantees that the investment chapter provides. The standards of treatment included in the US Model-BIT, and those of several other developed non-EU countries, apply to both pre- and post-establishment rights.\footnote{Prof. Dr. Tietje and Associate Prof. Dr. Baetens and Ecorys Rotterdam, “The Impact of Investor-State-Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership” [2014] Study prepared for the Minister of Foreign Trade and Development Cooperation, Ministry of Foreign affairs, The Netherlands para. 218.} This approach creates additional discussions on market access, more so than the post-investments-only approach.\footnote{Indeed, also covering the pre-establishment phase of investments in the FTA whilst also including ISDS provisions may create a risk of a shockwave of claims, if domestic measures to protect sensitive industries are in place.} Here, states can negotiate on the basis of positive lists, which only name the sector to which foreign access is allowed, or negative lists, which only comprise of the banned sectors, for example for national security reasons.

10.4 From a legal perspective, once a country opens up (parts of) its market to foreign investors on the basis of an international investment agreement, it must ensure the observance of the standards of treatment included therein. After all, that is the idea of such agreement in the first place. Traditionally, observing these standards has been most often ensured by including solid ISDS-provisions. ISDS as such should therefore not affect a country’s considerations on the extent to which it will open its markets to foreign investors. The market access question precedes the overall question in granting standards of treatment to foreign investors at all. That, however, is a complicated policy question to be answered differently per country based on a mix of factors. The concerns that follow from a country’s specific situation can be addressed by careful drafting of inter alia the definition of investment and of services, working with positive or negative lists and by enacting or amending additional, non-discriminatory national legislation regarding critical markets. For example, national investments by subsidiaries of foreign investors in health care or education could be addressed by putting in place laws dealing with ownership and management of investments in those markets, requiring e.g. a minimum of 51 per cent domestic ownership or a majority of nationals in the management board.

**Conclusion**

10.5 Granting internationally recognised standards of treatment, such as non-discriminatory and fair and equitable treatment, to foreign investors via an international investment agreement may raise questions regarding the extent of market access for those investors. The inclusion of ISDS provisions – a standard practice will not grant additional market access to foreign investors. Market access is a legitimate policy matter influenced by various factors that are
weighed differently by each government. Where different treaty practices on market access and investment protection meet, the success of the negotiations will depend on the contracting states’ willingness to overcome hurdles by finding creative solutions and effective drafting. The recently published agreement between Canada and the EU (CETA), in which the ISDS provisions are explicitly intended to only apply to established investments, may serve as an example in that regard.

Criticism 11: Despite absence of investment treaties, foreign direct investments flow into countries like Brazil

11.1 Virtually all countries worldwide, whether a developed or developing one, seek to increase FDI levels with the aim of financing public infrastructure projects, bringing capital, technology, know-how, and access to new products and markets. As a general rule, policy- and law-makers believe that FDI will help improve the countries’ productive capacity by benefitting from the global economy. Accordingly, in recent years, the proliferation of IIAs has been the result of the fierce competition for FDI inward flows and the protection of the country’s investors abroad.

11.2 Against this background, an important public policy debate has focussed on whether IIAs help attract FDI flows, particularly, to developing countries and the potential impact of IIAs to FDI flows.

11.3 Critics of the system have pointed out that countries, such as Brazil without an IIA relationship with their partners, are still major recipients of FDI flows from these very same countries. While this fact highlights the relevance of other FDI determinants, for instance existence of natural resources, regulatory and institutional framework as well as sound domestic policies, the whole picture should be put into context. Any debate must depart from the assumption that clear and enforceable rules established by international agreements in order to protect foreign investors reduce political risks and thereby increase the attractiveness of host countries.123

11.4 Although their prime role is to add an international dimension to investment protection and foster transparency, predictability and stability of the investment framework in host countries, IIAs undoubtedly impact FDI inflows by guaranteeing foreign investors a minimum standard of treatment and providing a mechanism for dispute settlement. As a result, IIAs reduce the risks associated

with investing abroad and provide a shortcut of the host country's credibility in the international arena. In the absence of IIAs, foreign investors attempt to balance their risk by either negotiating longer concession agreements or much higher returns in the shorter term.

11.5 Studies in relation to the impact of IIAs on FDI, despite the existent limitations related to data constraints and methodological challenges, have provided very heterogeneous results. However, as a common feature, none of these studies have determined that IIAs have a negative effect on FDI flows. On the contrary, the majority of dissertations on this field have concluded that IIAs, and specifically BITs, do promote inflow levels of FDI. For example, the U.S. share of FDI stock in Brazil, China, India or South Africa ranges between 5 and 15 per cent, which is considerable lower to the U.S. share in global inward FDI stock (i.e. around 25 per cent). Indeed, a recently published study by the Dutch statistical office has found that FDI flows increase by 35\% after the ratification of a BIT.

11.6 All of the above suggests caution with respect to drawing direct conclusions when criticizing the relevance of IIAs or BITs on the decision by companies to invest in a given country. A survey of 602 transnational corporations conducted for UNCTAD during the first half of 2007 on whether the existence of an international agreement (for instance, a BIT) may influence the company's decision on which market to invest in, gave the following outcome:

- 24\% of responses – "to a very great extent"
- 48\% of responses – "to a limited extent"

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• 23% of responses – “do not use them at all”
• 9% of responses – “do not know”

11.7 That would mean that, for an overwhelming majority of companies, the existence of IIAs that have entered into force remain important in order to make an investment decision. The same survey concluded that IIAs, specifically BITs, ranked in the middle of FDI determinants for developing countries. The most important factors identified by the survey affecting investment decisions by transnational corporations were (i) the host country's macroeconomic and political stability; and (ii) the country’s regulatory and institutional environment’s strength.

11.8 Additionally, IIAs and BITs particularly matter for SMEs, which unlike powerful transnational corporations, do not have the ability to negotiate individual investment contracts with host governments. Evidence of this is the fact that a significant number of investment arbitration claims were submitted by such smaller companies.¹²⁸

11.9 Any potential impact of international, bilateral or regional, agreements with investment provisions in attracting FDI should be seen in the context of a myriad of determinants. Key among these is the economic attractiveness of FDI recipient countries because of (1) their market's size and growth rate, (2) average income per capita, (3) the availability and costs of raw materials and natural resources, as well as (4) other factors (skills, cheap labour, infrastructure, etc.) and (5) the institutional characteristic of the host country (its judiciary system, red tape and corruption levels).¹²⁹

11.10 The challenges to enhance the attractiveness to FDI within the public policy arena have led to a situation where countries decide to pursue different paths. The decision on which path to follow, and whether or not to have IIAs as part of it, is a matter of choice for governments which need to consider a number of factors. These factors may include the level of the country's economic development, geopolitical characteristics, trade and investment comparative advantages and the general approach to bilateral or regional cooperation.

11.11 Indeed, Brazil very recently has signed new generation BITs with Mozambique and Angola.¹³⁰ While, these BITs do not include the classic ISDS provisions, they contain a whole toolbox of dispute avoiding and dispute resolution tools. These BITs prove that even Brazil considers it necessary to create an international legal framework - mainly with a view to support its investors, who are investing increasingly abroad.

Conclusion

To conclude, investment treaties are an important tool for States in attracting FDI. Of course, they are not the only instruments to attract FDI and States may well choose not to enter into them and still have a stable and attractive investment climate. One thing that can be said though is that none of the studies available have found that IIAs have a negative effect on FDI flows. In any case, investors normally perfectly know how to calculate risks and investment treaties with ISDS provisions are one - important - factor of this calculation.

General conclusion and outlook

It seems that the current heated debate in Europe regarding the EU’s investment policy is comparable to what the US went through in the past decade when it updated its model BIT text of 2004, and more recently of 2012. Hence, Europe is experiencing the same growing pains when calibrating its investment policy as the US. However, the situation of the EU is much more complicated because of the fact that in the previous 50 years it were the Member States which developed individually their investment policy by concluding about 1,500 BITs with the rest of the world.

The European Commission is now entrusted with the difficult task of developing an EU investment policy that must take into account numerous interests and satisfy divergent or even conflicting demands from parliaments, NGOs, trade unions, business associations etc.

At the same time, the EU and its Member States are going through a serious economic and financial crisis, which requires new significant efforts to stimulate investments and create jobs. Indeed, in order to jump start the EU’s economy, Commission President Juncker has proposed a bold Investment Plan of €315 billion, which to a large extent must come from private investors.

Also, it should be recognized that the position of the EU and its Member States as a mainly FDI-exporting region has changed into an equally important FDI-importing region. In other words, whereas in the past Member States were almost exclusively interested in promoting and protecting their own investors and investments abroad, nowadays, the right to regulate and the perceived need to defend themselves against foreign investors is gaining importance.

It is in this politically, economically and legally very complex environment in which the current investment policy debate is taking place in Europe.

Accordingly, it is an absolute necessity to make informed decisions based on facts rather than myths.
This EFILA paper is a serious contribution for an informed decision by providing an in-depth analysis of the main criticisms, which have been voiced against the current investment law and arbitration system.

The bottom line of this analysis is that most of the criticisms are neither supported by the facts nor by the treaty practice and case law.

The fact is that the system has been functioning satisfactorily and that it generally provides for adequate resolution of investment disputes.

Moreover, it has been shown that BITs and ISDS are important instruments for promoting FDI and thereby jobs, promoting the Rule of law worldwide and protecting the legitimate rights and expectations of investors. These are the necessary elements for a balanced and responsible investment policy, which benefits both States and investors alike.

At the same time, it must be acknowledged that the system is not perfect – as no legal system is perfect. Accordingly, the system and the users of the system – States, investors, arbitrators, lawyers and academics – have been and continue to improve the system incrementally. This has been in particular the case regarding increasing the transparency of arbitral proceedings and the tightening up of the codes of conduct for arbitrators and requiring higher standards for impartiality and independence.

Obviously, if States and their constituencies so demand, more incremental improvements of the system can be introduced. However, as this analysis has shown, investment arbitration is so beneficial for States and investors alike that it would be irresponsible to eliminate it.

In conclusion, it is important to distinguish between facts and myths and take informed decisions after carefully balancing all the pros and cons.

EFILA considers this analysis to be an important contribution to an informed debate and decision-making process.

EFILA welcomes any comments and questions on this paper and remains committed to continue its efforts also in the future.

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