

# **The Rapidly Changing Situation in Investment Agreements**

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# The investment protection system problematique

- **Imbalanced and often vague treaty provisions**, focus on the investors' rights and neglect investors' responsibilities, lack of express recognition and safeguard of host states' regulatory authority, allowing for expansive interpretation by arbitrators.
- **Flawed investor-state dispute settlement mechanism**, led by a network of arbitrators dominated by private lawyers whose expertise often stems from commercial law, and often exhibiting conflict of interest.
- **Far reaching enforcement rules of arbitral awards**, under the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards (1958)- currently 154 Members.

# Selected problematic provisions in investment treaties

- **Broad scope and definition of protected investor and investments** → extends to cover “every kind of asset” or “any kind of asset”, extending protection to intangibles (mortgages, intellectual property rights, shares, stocks and similar forms of participation in companies, expectations of future gains and profits).
- **National treatment**
- **MFN** → used by investors to claim equally favourable treatment as the host country offers under other BITs to investors of any other country.
- **Fair and equitable treatment** → most frequent claim in ISDS, nearly 75 percent of ISDS cases under US IIAs have found FET violations, became a “catch all” clause interpreted to cover loss of future expected profits.
- **Indirect expropriation** → under the expansive approach to interpreting ‘indirect expropriation’, any regulatory measure- such as ones dealing with production processes, or technological addition, or ban on harmful material- could be judged as indirect expropriation. Such an approach could have the effect of causing a regulatory chill at the national level.
- **Repatriation of profits or free transfer of capital** → freely transferable without unreasonable delay on a non-discriminatory basis, at the prevailing market exchange rate on the date of the transfer, and to be fully convertible to the currency in which the investment is made or in any convertible currency
- **Survival clause** → extends the protections granted and consent to international arbitration under the treaty after it is terminated (some cases for 20 years)
- **Investor-state dispute settlement clause**

# Push for pre-establishment rights & prohibition of performance requirements

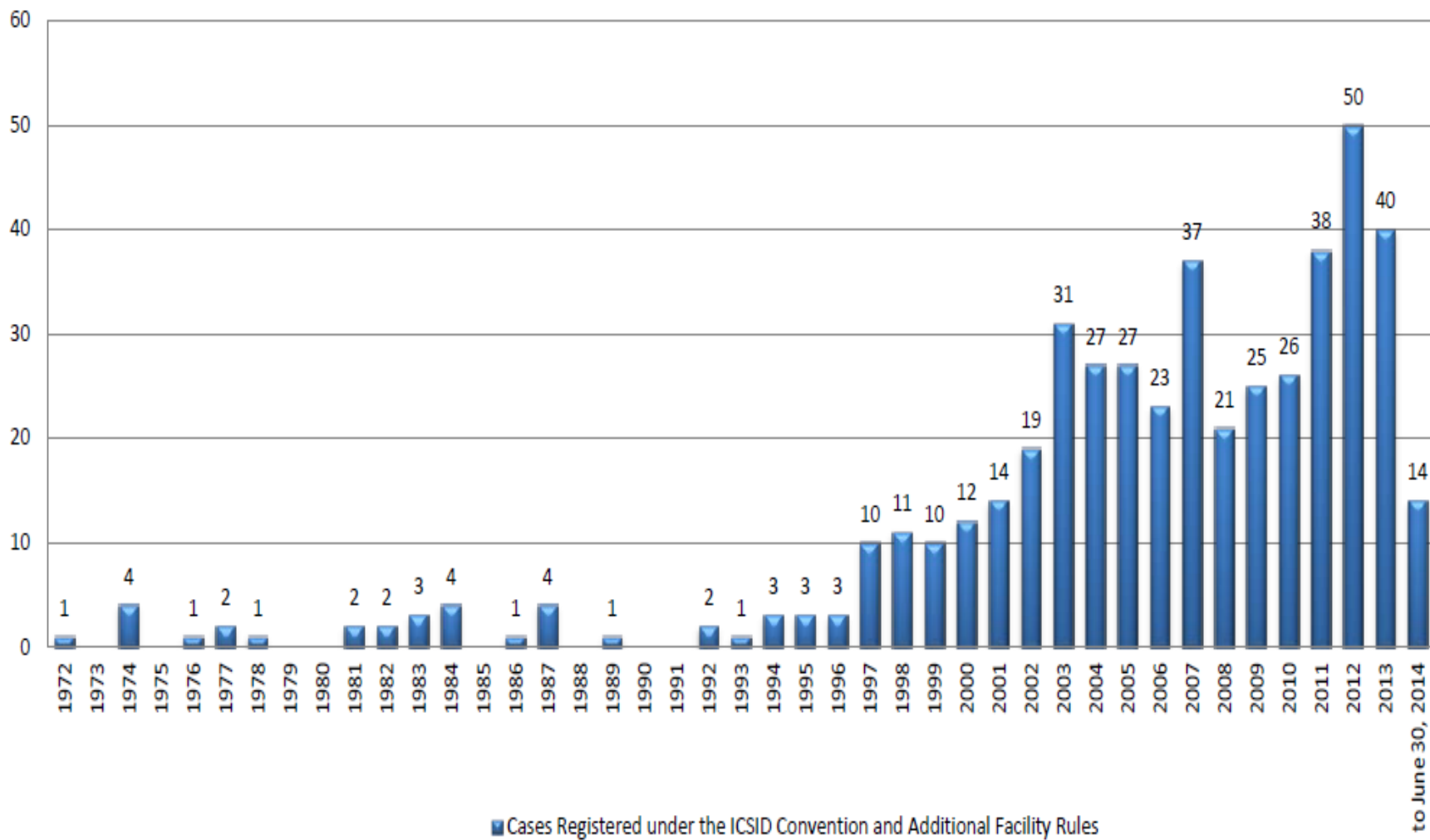
- **Pre-establishment rights:** extends national treatment and MFN treatment to the “establishment, acquisition and expansion” of investments → each Party allows investors of other Parties to establish an investment in their territory on terms no less favorable than those that apply to domestic investors (national treatment) or investors from third countries (most-favored-nation treatment)
- **Prohibition of PRs:** much wider net of prohibitions on major policy tools compared to TRIMS (such as entering joint ventures with local companies, employing certain percentage of local workers, transfer of technology, or contribution to research and development....)

# A system still in expansion

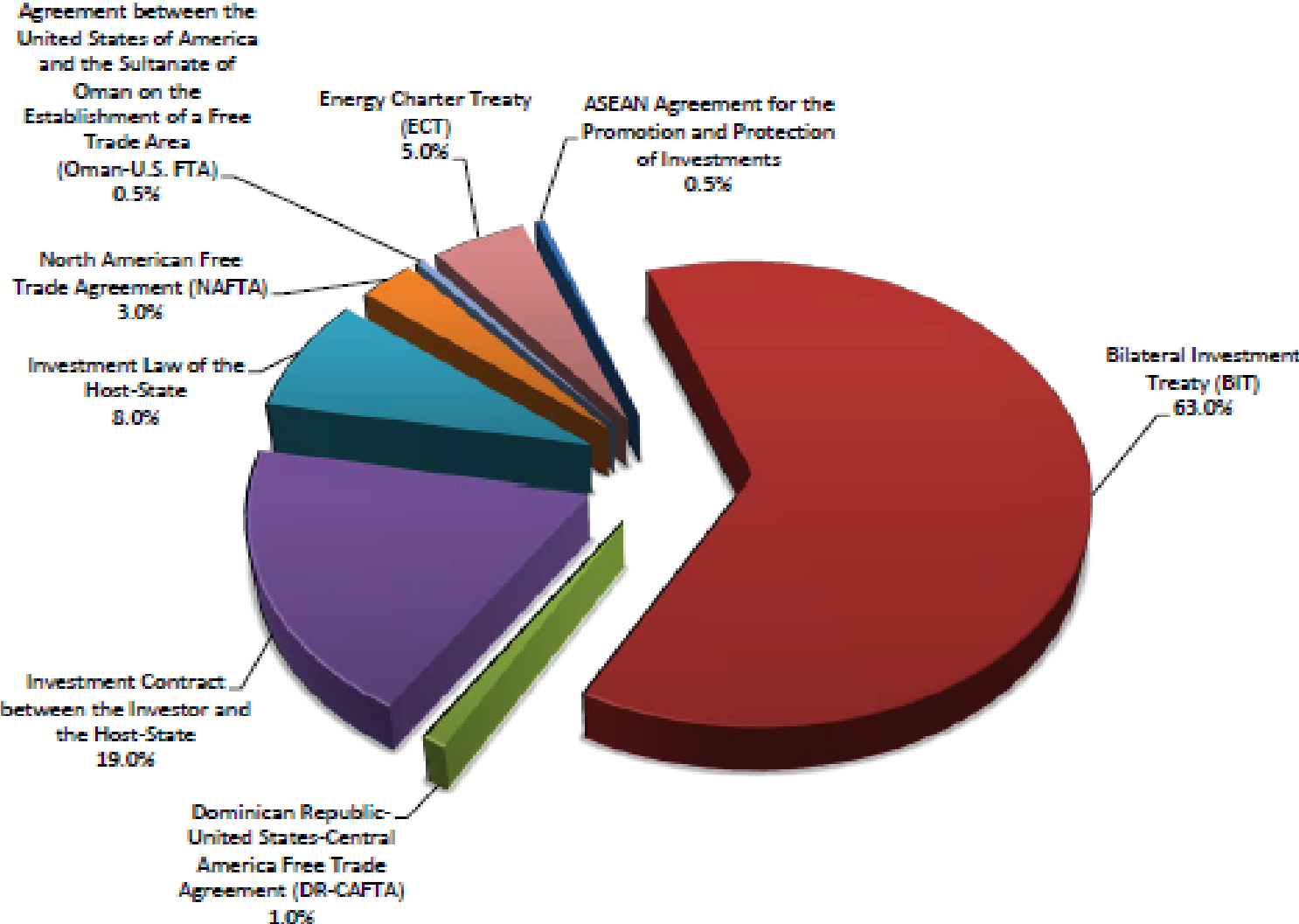
- **New agreements:** 44 new IIAs in 2013, and 27 in 2014 (Source: UNCTAD WIR 2014).
- **ISDS cases:** 98 States have been respondents in a total of 568 known treaty-based cases (Source: UNCTAD).
  - 56 new known investment treaty claims were filed in 2013, second largest number of known cases in a single year, and 42 new known claims in 2014
  - Investors from the European Union and the United States are the most frequent users of the ISDS system.
    - ✓ European investors estimated to have filed more than half of investment arbitration claims = around 300 cases of known arbitration claims (Source: CSIS).
    - ✓ The Netherlands (61 cases), the United Kingdom (42 cases), Germany (39 cases)
    - ✓ The United States and EU investors account for 75 % of the global number of known ISDS claims (Source: UNCTAD, 2014).

# A system still in expansion

*As of June 2014, ICSID registered 473 cases (Source: ICSID 2014)*

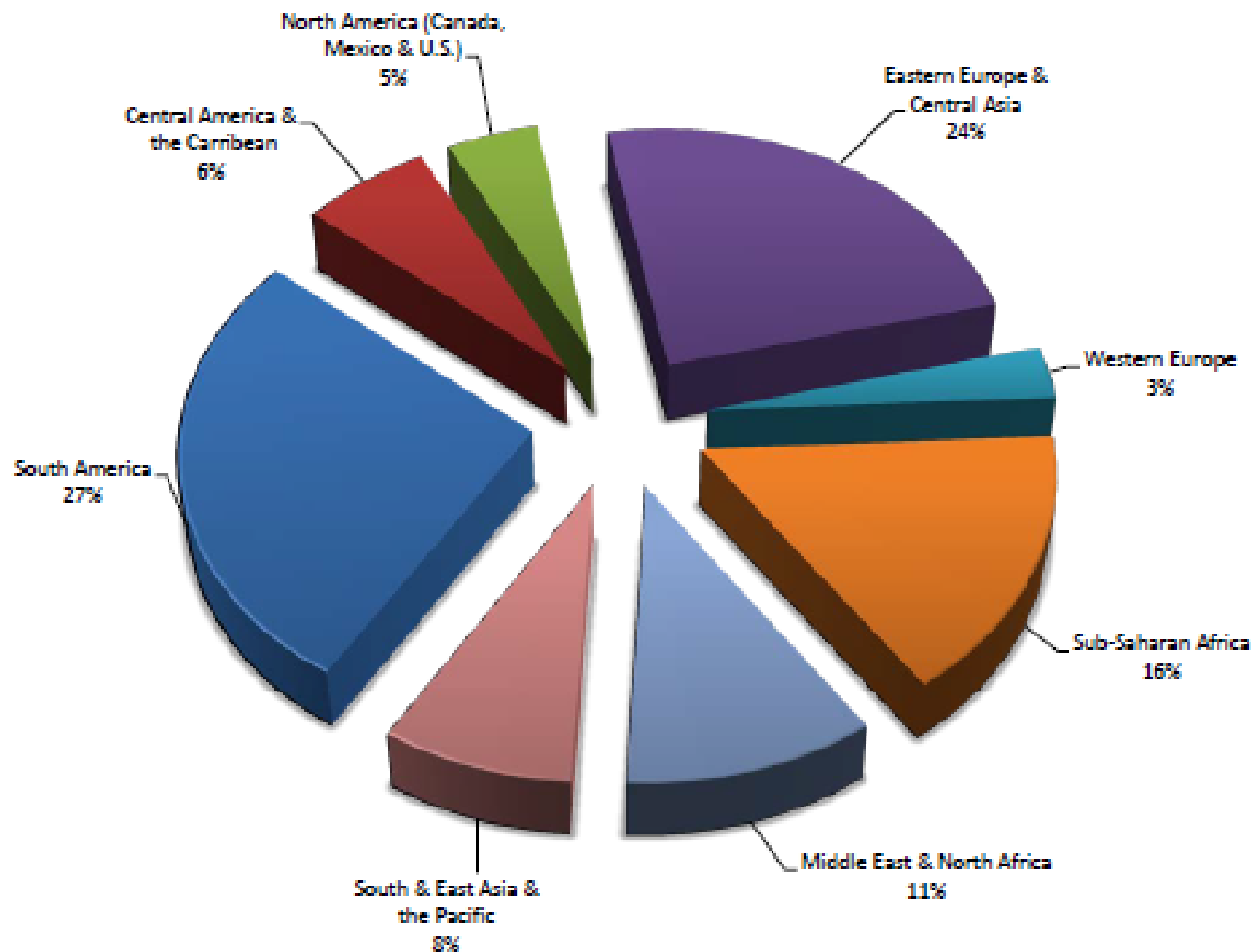


# BITS are by far the most frequently used basis of consent invoked to establish ICSID jurisdiction (Source: ICSID 2014)





## Geographic distribution of all cases registered under ICSID Convention and Additional Facility Rules (by State Party, source: ICSID 2014)

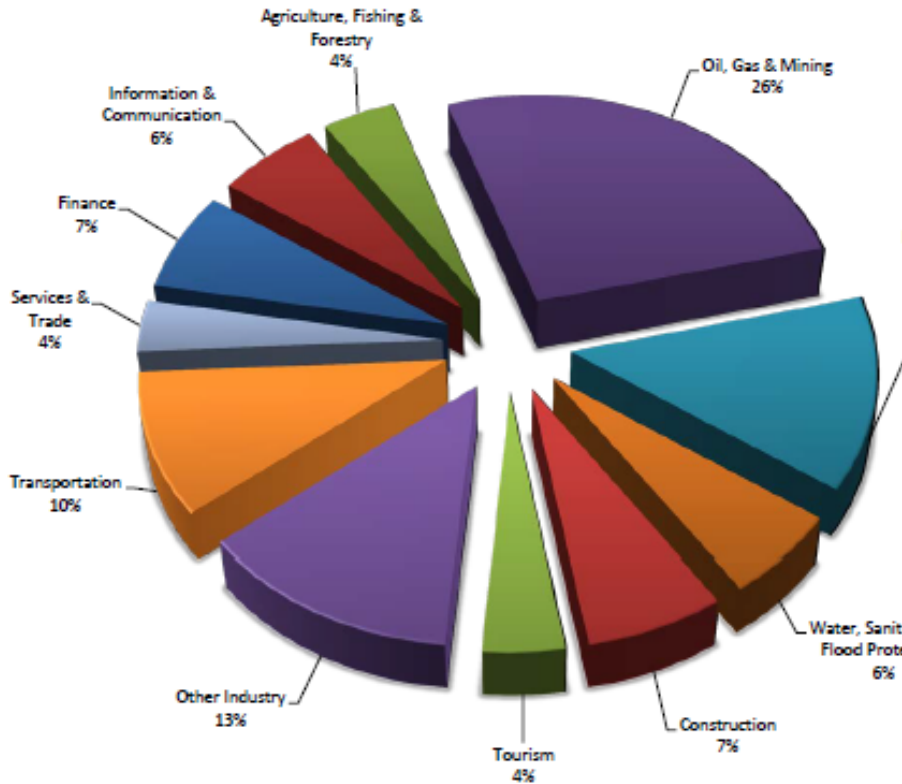


# Using ISDS to challenge regulatory measures

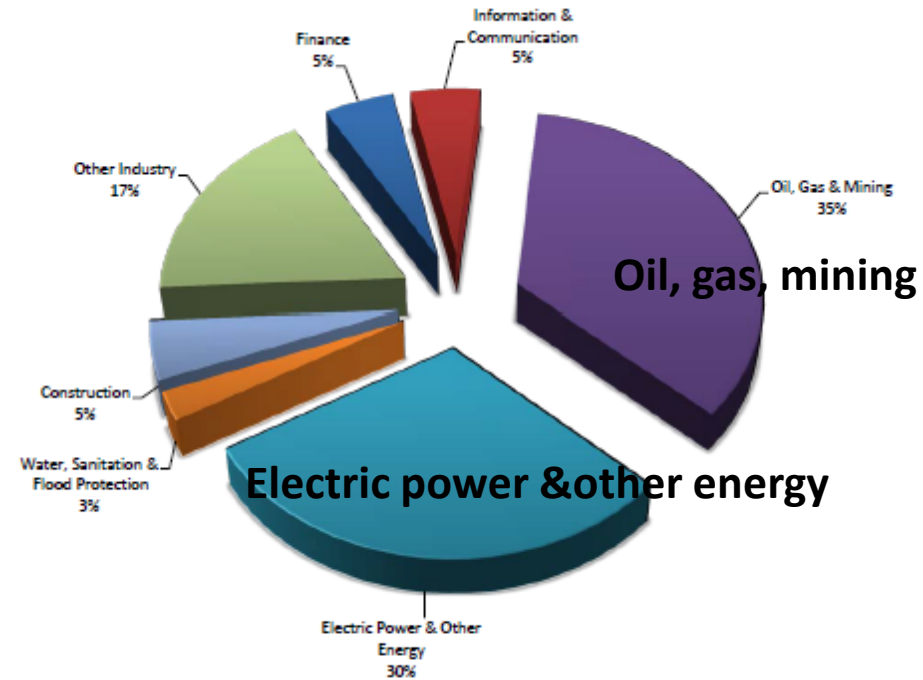
- Bank regulators' response to the global financial crisis (Ping An v. Belgium)
- Debt restructuring (Cyprus Popular Bank v. Greece)
- Ban on nuclear power after the Fukushima meltdown (Vattenfall v. Germany)
- Land reforms (Border Timbers v. Zimbabwe)
- Division of spoils between countries (Sudapet v. South Sudan),
- Economic relations/ labor policies (Maiman v. Egypt and Veolia v. Egypt)
- Actions by the Supreme Court and Central Bank (Duetsche Bank v. Sri Lanka).
- Health and medicines and tobacco regulations: Eli Lilly v. Canada (patents),; Philip Morris v. Australia (tobacco), and Philip Morris v. Uruguay (tobacco); Ethyl v. Canada (toxic gas additive), settled (resulted in payment to investor and toxics ban reversed ).
- Environmental regulations: Vattenfall v. Germany I (coal); Lone Pine v. Canada (on fracking); Chevron v. Ecuador; Renco v. Peru (metal smelter pollution); Metalclad v. Mexico (toxic waste); S.D. Myers v. Canada (toxic waste).

As well as regulations in the areas of waste management, mining, public safety, financial regulations, labor, agriculture, public services....

# Distribution of all cases registered under ICSID Convention and Additional Facility Rules (overall and in 2014) (Source: ICSID 2014)



Overall



In 2014

## Awards are increasing in size

- Yukos v. Russia-- **USD 50 billion** (3 awards for 3 former Yukos majority shareholders, 2014)
- Occidental v. Ecuador – **USD 1,769,625,000** (ICSID, 2012)
- Al Kharafi and Sons v. Libya-- **USD 935 million** (ad hoc, 2013, with interest, fixed at 4% per annum, the sums owing under the March 22, 2013 award are increasing, topping one billion US dollars at the end of 2014)
- Gold Reserve v. Venezuela -- **USD 713 million plus costs** (ICSID, 2014)
- Wagih Siag v. Egypt—**74,550,795 USD** (ICSID, 2009)
- Duetsche Bank v. Sri Lanka—**USD 60,368,993** (ICSID, 2012)
- Bernandus Henricus v. Zimbabwe-- **USD 10,637,000** (ICSID, 2009)
- France Telecom v. Lebanon- **USD 266,349,600** (UNCITRAL, 2005)
- Argentina— **USD 1,140,819,547** in 15 cases

# The dynamics of the discussion on reforms

Suggestions on ISDS	On substantive treaty content
<ul style="list-style-type: none"><li>➤ Clarify the scope of who may bring what dispute to ISDS</li><li>➤ Rely more on the local legal system (exhaustion of local remedies, fork-in-the-road, primacy of domestic court..)</li><li>➤ Mutual consent on case by case basis</li><li>➤ State-to-State dispute settlement modality</li><li>➤ Standing international investment court</li><li>➤ Appeals facility</li><li>➤ Transparency of arbitration</li><li>➤ Alternative mechanisms, such as mediation and conciliation</li><li>➤ Regional Investment Dispute Resolution Centers</li><li>➤ Additional guidance to tribunals, clarifying the obligations that States intended to adopt through IIAs</li></ul>	<ul style="list-style-type: none"><li>➤ Re-negotiate IIAs</li><li>➤ Creating a pattern of renegotiations</li><li>➤ Consider a new generation of investment provisions, on sustainability, responsible investments “promoting” the flow of productive investments</li><li>➤ Review the IIA model</li><li>➤ Limit the scope of coverage</li><li>➤ Review and clarify provisions in IIAs</li><li>➤ Establish widely accepted guidelines for interpretation of certain standards</li><li>➤ Design applicable and appropriate exceptions to guarantee regulatory space for public policies</li><li>➤ Add clarification of the state intentions through an annex</li><li>➤ Move towards productive investments facilitation and promotion model</li></ul>

# Highlights from countries seeking reforms & alternative approaches

- Reviewing BITs, establishing an Inter-Ministerial Committee to oversee work, consulting with other national and international stakeholders (civil society, private sector, academics, lawyers...)
- Terminating existing BITs, by not renewing BITs that expired, giving due notice of non-renewal within the stipulated period of notice before the expiry date of the treaty (*UNCTAD have noted that by the end of 2015, more than 1,457 BITs out of 3,268 existing treaties*)
- Deleting the survival clause before terminating the treaty
- Clarifying investment protection standards in a new national Investment Act
- Revert to investment contracts as the main legal instrument defining the relation with investors, including clear obligation on the investor such as performance requirements
- Develop a new model BIT, adopting the approach “Investment for Development” or “Promotion and Facilitation of Investment”
- Denounce ICSID (*leads to ‘de facto’ termination of investor-state dispute settlement under BITs which stipulate ICSID as the only forum for arbitration*)

# Key questions in the way forward

- Is it enough to add provisions related to sustainable development and corporate social responsibility to the current models of investment treaties?
- Should not reform efforts start from the fundamental question of whether States need investment protection treaties to attract productive investments and provide foreign investors with the guarantees they need
- Are there are alternatives- such as national laws- that States could revert to?
- Do we need a more comprehensive approach through withdrawal from these treaties or renegotiations with a view to establishing treaties that safeguard the right to regulate of the State and balances between rights and responsibilities of investors?
- What role should ISDS play, and are there specific types of investment disputes that should fall under the purview of international courts and tribunals and others that should only be dealt with between the home state and the host state, or through national courts?
- Can an approach similar to the one adopted in the UNCITRAL context be a viable route to undertake substantive reforms in the IIA regime? whereby states adopted a convention on transparency in treaty based investor-state arbitration that extends its rules to both existing and future investment treaties.

# South Centre Program on Investment Policies and Treaties

We would be glad to hear from you on ways we can work with your missions and capitals:

- Research and analysis
- Advisory services on legal and economic issues related to investment policies and treaties
- Organizing meetings to promote discussions on rethinking investment protection regime and ISDS
- Support to national or regional processes to review and reform the investment protection regime



# What do investors seek?

**According to World Bank study:** “both a review of the empirical literature and analysis using new data sources suggest that business opportunities—as represented by, for example, the size and growth potential of markets—are by far the most powerful determinants of FDI”.

**According to UNCTAD TDR 2014:** “Using one methodology results indicate that BITs have a positive impact on bilateral FDI although the estimated magnitude of this impact is small...an alternative method showed that BITs appear to have no effect on bilateral North-South FDI flows....results do not support the hypothesis that BITs foster bilateral FDI. Developing country policymakers should not assume that signing up to BITs will boost FDI..they should remain cautious about any kind of recommendation to actively pursue BITs” (See TDR 2014, p. 159)

**Surveys of investors and political risk insurers:** exceedingly rare for foreign investors to factor in investment treaties (including liberalization agreement) when committing capital abroad, and availability and pricing of public and private political risk insurance is very rarely affected by presence or absence of an investment treaty.

**Situation in South Africa:** ranked by UNCTAD as the top recipient of FDI inflows among the African countries in 2013.

**Situation in Bolivia:** FDI inflows have steadily increased, reaching an unprecedented peak of US\$1.75 billion in 2013.

# The discussion in the EU

*Versus the European approach to negotiations with developing countries*

- **Cecilia Malmström, the newly appointed EU Trade Commissioner:** *“It is indeed a very toxic issue in this parliament and elsewhere...I agree that there are problems with ISDS because there have been abuses”* (Appearing before the European Parliament for her confirmation hearing commenting on ISDS).
- **Social and Democratic (S&D) block in the European Parliament:** *“The S&D Group in the European Parliament will oppose the introduction of an investor-state dispute settlement (ISDS) in the Transatlantic Trade and Investment Partnership (TTIP) currently being negotiated by the EU and the United States”* (Press statement).
- **Parliamentary State Secretary for Germany’s Ministry of Economics and Energy:** *“We believe it must remain possible for national governments to act, to enact legislation in [the] future, and the agreement cannot undermine that, [...] We cannot just be forced to accept that, thrust down our throat.”* (Commenting on the EU-Canada Trade Agreement and inclusion of a provision on ISDS)
- The European Commission public consultation on TTIP- 150,000 responses between 27 March and 13 July 2014)

→ **Should there be double standards in approaching the sovereign right of the state to regulate?**

# Selected Quotes

- **Quote from investment arbitrator Gabrielle Kaufmann-Kohler (2005)** : “We all know that investment arbitration is booming. We also know that it has come under heavy criticism lately, from NGOs, media and certain governments. Arbitral tribunals are "shadow governments" dispensing "justice behind closed doors" and even sometimes engaging in "arbitral terrorism". Although these formulations are certainly excessive, they nevertheless reflect a legitimate concern. Investment arbitration is based on the model of commercial arbitration, yet it differs from most commercial arbitrations by one significant element: investment arbitration often involves issues of major public interest. This public interest cannot remain without influence on the process. It calls for transparency in the proceedings and consistency in the results. Transparency is about opening the doors of the hearing room. Consistency is about delivering coherent decisions and avoiding contradictory results that undermine the credibility of investment arbitration overall and jeopardize the development of investment law”.
- **Chevron’s Comments on TTIP to USTR**: “A TTIP with strong and comprehensive investment provisions could set the global standard for investment protection now and into the future [...] To truly operationalize this standard, Chevron urges that, once negotiated, it be extended over time to future trade, investment or other related agreements to move us towards a globally-consistent, strong and comprehensive standard for investment protection [...] Investor-State arbitration is a concept that is being challenged by some governments today as an unwarranted infringement on their sovereignty. In fact, these dispute settlement provisions ensure that neither side has the power to unduly influence determinations of law and fact by assuring access to a neutral forum for resolving disputes.”