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The Cooperation and Facilitation Investment Agreement (CFIA) in the context of the discussions on the reform of the ISDS system

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The Brazilian Cooperation and Facilitation Investment Agreement (CFIA) model establishes an alternative approach to dispute resolution[1]. This does not mean, however, that the CFIA is silent with regards to possible disputes arising from breaches to the agreement and/or claims by investors. Based on the premise that the investment regime between two or more countries is a positive-sum game, in which all parties involved win, the CFIA presents an approach based on the prevention of disputes. The present brief aims at explaining how the Brazilian model can contribute to the discussions on the reform of the investor-State dispute settlement mechanism (ISDS) system, or of dispute resolution in International Investment Agreements (IIAs) as a whole. The CFIA is, to a great extent, a response to what the Brazilian Parliament interpreted as the shortcomings of the traditional bilateral investment treaty (BIT) models. The first part of the text will examine the context of the discussions that prevented Brazil from ratifying the few BITs signed in the 1990s and the conjectural changes that led to the elaboration of an alternative IIA model. The second part will detail the emphasis on prevention of disputes that is inherent to the CFIA. In its third part, the present text will explain the specific provisions of the CFIA regarding the settlement of disputes at the State-to-State level (SSDS).

As put by Cozendey and Cavalcante[2], the Brazilian model departs from the traditional view of IIAs that protection of foreign investment equals promotion of such investments by promoting a long-term perspective that states should cooperate in order to help the attraction and expansion of reciprocal investments. The CFIA advocates the institution of mechanisms that facilitate the access of foreign investors to the national market. Moreover, it emphasizes the need for cooperation as a determining factor for attracting investments. More important to the present discussion, the CFIA is a response to the demand for a review of traditional BITs, especially in relation to ISDS.

Brazil negotiated and signed 14 BITs in the 1990s (with Germany, Belgium and Luxembourg, Chile, South Korea, Cuba, Denmark, Finland, France, Italy, Netherlands, Portugal, Switzerland, United Kingdom and Venezuela). The National Congress did not approve the negotiated texts, and, in accordance with the Brazilian Federal Constitution´s provisions regarding the role of the Legislative in the process of treaty making (article 49, I)[3], the ratification of the mentioned BITs was stalled, and their texts were removed from consideration by Congress.

In a recent study by Vivian Rocha Gabriel[4], several reasons for the refusal of BIT approval by the National Congress were identified. In the first place, the provisions on the payment of compensation for expropriation without undue delay in freely convertible currency[5] were considered unconstitutional. In Brazil, there are two possibilities in which the national investor is not entitled to liquid and immediate payment, namely those related to the expropriation of underused or unused urban soil that do not provide for the social functions of the city and expropriation by social interest for the purpose of agrarian reform. In both cases the compensation is made through specific titles, as established respectively by articles 182, para. 4, III, and 184 of the Federal Constitution. Secondly, Brazilian legislators argued that the commitment of immediacy and liquidity

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While the reform process of international investment protection treaties is evolving, it is still at a nascent stage. Systemic reforms that would safeguard the sovereign right to regulate and balance the rights and responsibilities of investors would require more concerted efforts on behalf of home and host states of investment in terms of reforming treaties and rethinking the system of dispute settlement.

Experiences of developing countries reveal that without such systemic reforms, developing countries' ability to use foreign direct investment for industrialization and development will be impaired.

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established by the BITs could disrespect the chronological order of payments owed by the government, as established by article 100 of the Constitution. Finally, with regards to the possibility of using ISDS mechanisms, it was argued that the principle of access to justice (i.e. domestic legal remedies) could be violated, thus hampering state sovereignty. It can be argued that the preservation of regulatory space is at the core of not only the Brazilian concerns related to BITs, but also of the drafting of the CFIA.

It is important to note that, in spite of its decision to abstain from ratifying traditional IIAs, Brazil increasingly became one of the world´s main destinations of foreign direct investment (FDI). According to the latest United Nations Conference on Trade and Development (UNCTAD) World Investment Report[6], Brazil remains among the top importers of capital, being the seventh largest receiver of FDI in 2016. Nevertheless, the country has undergone a significant change since the early 2000s: it also became an exporter of capital, as an increasing number of Brazilian companies went through a process of internationalization.

In this context, efforts were made at the Executive level of Government to develop an IIA model that would, on the one hand, respect the issues related to national sovereignty raised by the Legislative and, on the other hand, offer Brazilian bureaucratic support for Brazilian investors' activities overseas. In 2012, the Foreign Trade Board (CAMEX), which is part of the Office of the President of the Republic, was given a mandate to develop an IIA model text, in consultation with both the public and the private sectors. In terms of safeguarding policy space, the three main issues considered problematic in traditional BITs were identified: the possibility of indirect expropriation, the protection of portfolio investments and the recourse to ISDS mechanisms.

Efforts have also been made both at the academic and the multilateral levels to clarify the meaning of indirect expropriation. The Organisation for Economic Co -operation and Development (OECD), for instance, has published papers on the relation between indirect expropriation and the right to regulate[10] and concluded that, although the determination of direct expropriation is a clear process, the identification of indirect expropriation "has required tribunals to undertake a thorough case-by-case examination and a careful consideration of the specific wording of the treaty"[11]. The fact that regulatory functions of the States relating to the protection of human rights, to national security and/or to the protection of the environment, for example, may be subject to requirements of compensation that would have to be decided on an *ad hoc* basis is considered by Brazil as a major hindrance to policy space.

The protection of portfolio investments has also proven to be a delicate issue in investment arbitrations, as it enhances the possibility of private interests (often related to speculative capital flows) clashing with the public interest. The CFIA makes it clear that only FDI can be subject to provisions of the agreement[12], as only an investment that has a clear impact on the development of the host country, such as FDI, should warrant being covered by an agreement. In terms of dispute settlement, the focus on FDI makes the CFIA a more technical legal instrument and, therefore, less prone to arbitral interpretations that may compromise social interests.

The demand for a reform of the ISDS system has gained momentum in the last couple of years: countries such as Bolivia and Ecuador have denounced their BITs; others are undergoing a process of revision of signed treaties and; at the multilateral level, the United Nations Commission on International Trade Law (UNCITRAL) has reinstated Working Group III with a mandate to discuss the possibility of reform of ISDS. As pointed out by the UN Commission, among the main concerns related to ISDS are: (i) procedural aspects; (ii) duration and cost of arbitration proceedings; (iii) transparency; (iv) appointment of arbitrators and double hatting (possibility of individuals being arbitrators and lawyers, as the case may be)[13]. For Brazil, such concerns reinforce the conclusion that ISDS can limit the regulatory space of states in as much as it allows for individuals to be subject of Public International Law not by reason of their guaranteed rights - such as in the international human rights regime - but by means of their private interests being safeguarded to the detriment of public interest. As the following sections elaborate on

CFIAs signed by Brazil[7]

Country	*Date of signature*	*Status*
Mozambique	30/3/2015	Awaiting ratification
Angola	1/4/2015	In force
Mexico	26/5/2015	Awaiting ratification
Malawi	26/6/2015	Awaiting ratification
Colombia	9/10/2015	Under examination by the National Congress
Chile	23/11/2015	Awaiting ratification
Peru[8]	29/4/2016	Awaiting ratification
MERCOSUR[9]	7/4/2017	Under examination by the National Congress

the prevention of disputes and the settlement of dispute provisions in the CFIA model, it is important to bear in mind that the Brazilian proposal aims at diminishing the political controversy of ISDS by emphasizing the relation between States that are parties to the agreement.

The CFIA model as a tool to prevent disputes

Due to Brazil's long standing criticism of the traditional BIT model, the country had a *tabula rasa* when the need arose to develop public policies to support the growing internationalization of Brazilian companies. As explained in the previous section, the CFIA tried to learn from the shortcomings of traditional BITs, especially in what refers to indirect expropriation, protection of portfolio investments and the ISDS system.

The new Brazilian model also brought a significant change as to what an international investment agreement should be. Traditional BITs have to a certain degree a "passive nature", as they have virtually no usage before a dispute arises between the parties. These agreements work as an insurance policy which is to be kept in some forgotten drawer and only used as a last resort, when the relation between the investor and the host State has already deteriorated significantly.

Extensive consultations with the private sector during the drafting of the CFIA model made it clear that Brazilian investors were not particularly interested in rules related to dispute resolution. Most of their investments were located in neighboring countries and natural markets for Brazilian companies, such as in the case of Portuguese-speaking countries. As it would be difficult for them to exit those markets, Brazilian investors were more interested in the facilitation of daily operations in new markets than having an insurance policy that they might be unwilling to use. There was no intention of poisoning long-term partnerships with the lengthy and costly litigations of ISDS cases as it would be the case if the insurance was to be used.

The CFIA innovates by making the prevention of disputes a core element in the effort of facilitating and promoting bilateral FDI flows. The agreements specify that each country must designate a focal point (or an ombudsperson), responsible for handling investment-related issues raised by investors of the other country. Those issues range from doubts concerning applicable law to available information on investment opportunities as well as complaints regarding delays to obtain required licenses. This role of the ombudsperson is sometimes referred to as "hand holding" of investors, as the ombudsperson has an active role in supporting any investor regarding investment-related issues.

After analyzing an issue raised by the investor, the focal point might re-direct the question or concern to the relevant agency(ies). For example, if an issue consists of delays in obtaining environmental licensing for a new commercial harbor, the ombudsperson would contact environmental authorities on behalf of the investor and verify the reasons of such delays. If no satisfactory answer or solution is found, the ombudsperson might bring the issue to the attention of a higher hierarchical level.

The Brazilian investment ombudsperson was inspired by the successful experience of the Korean Foreign Investment Ombudsman. According to its institutional website:

> "The Office of the Foreign Investment Ombudsman, which was established in 1999, aims to resolve the grievances of foreign-invested companies operating in Korea.
>
> The Foreign Investment Ombudsman is commissioned by the President of the Republic of Korea and the OFIO operates a "Home Doctor" system under which specialists from various fields, such as finance, accounting, law, industrial sites, taxation, law etc., provide foreign-invested companies one-on-one service by investigating and resolving a wide range of grievances in the most efficient and effective manner. … With years of grievance resolution expertise cases, the OFIO works to prevent problems and improve Korea's investment environment."[14]

Brazil was particularly interested in replicating the procedure of addressing grievances resulting "from inadequate laws or administrative hindrances on the part of the Republic of Korea Government", what would enable the Korean investment ombudsperson to venture "beyond advising the investor by addressing the relevant Republic of Korea Government authorities and agencies directly to advocate improvements in investment policy, administrative procedures or laws and regulations."[15] According to the Korean approach, by creating a focal point to handle investors' issues within the government, possible internal coordination failures can be addressed and solved before they turn into disputes.

However, the dispute prevention features of the CFIA are not based exclusively on national investment facilitation institutions. The agreements also provide for the creation of joint committees, composed of both parties to the treaty, in order to promote investment and prevent disputes. The joint committee - which is supposed to meet regularly - aims to establish a high-level venue to prevent investment-related disputes and to share investment opportunities between the two parties, to foster the matchmaking of investors and investment opportunities and to exchange useful information for investment, such as new legislation, governmental bidding processes and public concessions.

The joint committee can also discuss issues of a previously defined "thematic agenda", such as visa facilitation for managers, executives and qualified employees, or licensing proceedings. This "thematic agenda" is tailor-made to each specific partner, seeking to find solutions to the concrete challenges faced by the investors of both sides. Once such difficulties are identified, the joint committee discussions can lead to the negotiation of new agreements to enhance bilateral cooperation.

Dispute settlement under the CFIA model

In the previous section, we have explained how and why

the provisions of the CFIA are designed to contribute to the prevention of disputes between foreign investors and host governments. Nonetheless, despite the efforts to settle grievances before they escalate into a full-fledged dispute, one cannot ignore that disputes between investors and host countries might occur. And the CFIA is not blind to this possibility.

While a traditional BIT is primarily dedicated to rules of ISDS as a means to provide the investor compensation in the case of breaches by the host government, the Brazilian approach focuses on dispute prevention mechanisms based on the bilateral dialogue through the focal points and the joint committee, responsible for the preliminary examination of specific issues brought by the parties. If a dispute leads to arbitration proceedings, the procedure will take place in the State-State format, much like the dispute settlement system of the World Trade Organization.

It is worth noting that the dispute settlement provision in the CFIA model is normally placed immediately after a specific provision on dispute prevention procedures. It is a clear sign of a last attempt of avoiding a dispute. This provision might take the form of consultations and direct negotiation between the parties[16] or it might be drafted in a very straightforward manner, as in the case of the MERCOSUR Protocol on Investment Cooperation and Facilitation[17]: when "a Member State considers that a specific measure adopted by the other Party constitutes a breach of this Agreement, it may invoke this Article to initiate a dispute prevention procedure within the Joint Committee"[18].

Although the provision is aimed at governments – and not at individual investors –, there is an underlying recognition that specific problems in the field of investment normally arise at the investor's level. That is precisely why individual investors affected by a measure might be invited to participate in the prevention of dispute procedure, so as they are granted an opportunity to present their point of view on the matter. Civil society can also participate in such proceedings, as the joint committee may invite other interested stakeholders to appear before the joint committee and present their views on such measure whenever relevant to the consideration of the measure in question. The records of the meetings held under the dispute prevention procedure and all related documentation will remain confidential, except for the report submitted by the joint committee, subject to the law of each of the Parties regarding the disclosure of information. In the Brazilian case, under Federal Law nº 12.527 of 2011, there is no perpetual secrecy regarding official documents, and the law defines the timeframe for disclosure of classified information.

The core objective of dispute prevention is to ensure that once a possible breach of obligations is identified the parties will work together to solve the problem and to restore the normality of the partnership between investor and the host government. The provision is designed to induce compliance.

The provision on the settlement of disputes between states parties kicks in only after "the procedure provided for in [the dispute prevention procedure] has been exhausted and the difference has not been settled"[19], a situation that allows the issue to be submitted "to the arbitration procedure between the State parties"[20]. The arbitration procedure might be set out according to the rules established in the CFIA[21] or could be referred to a permanent arbitral tribunal[22]. The provisions make it also clear that the objective of the arbitration procedure is to bring the measure found to be in breach of the CFIA to conformity[23].

It is worth noting that not all provisions of a CFIA are subject to arbitration procedures. For instance, provisions on social corporate responsibility, security exceptions and measures against corruption, measures affecting health, environment and labor are explicitly excluded from any dispute settlement under the Agreements.[24]

Although the purpose of the arbitration procedure is basically the same as of the dispute prevention – to induce compliance of measures found to be in breach of the CFIA –, in at least one case Brazil and the other party recognized that, if agreed by both parties, arbitrators could be allowed to conclude that there is damage to the investor that has to be compensated[25]. In other instances, Brazil and the other party to the CFIA made it absolutely clear that the arbitral tribunal shall not award compensation[26].

With regard to the measures covered by the CFIA, it applies only to measures adopted after the entering into force of the Agreement, leaving any previous measure outside the scope of application of the CFIA[27]. Another limitation to the dispute settlement procedure of the CFIA relates to the sunset clause embodied in the Agreement: no claim may be submitted to the dispute settlement mechanism if a period of more than five years has elapsed from the date on which the investor first had or should have been aware of an alleged breach of the Agreement for the first time.[28]

In sum, the CFIA approaches investment relations as state-to-state interactions, in the form of State-to-State dispute settlement (SSDS). The agreements establish an institutional framework responsible for managing its implementation and for addressing complaints that can emerge therefrom. They provide for channels to investors and other interested parties whose views and inputs might be relevant in managing a given investment relation. By concentrating in the hands of the states the decision to proceed with third-party dispute settlement, the CFIA could be challenged as a departure from the goal of "de-politicization" of disputes that allegedly underpins the BIT preference for ISDS mechanisms. Nonetheless, the dynamics of the CFIA is not so different from that of the WTO, where disputes are subject to (diplomatic) consultations followed by state-to-state dispute settlement. Yet, one does not often hear that the WTO system is "politicized" because affected private parties are not granted *locus standi*.

Endnotes

[1] Felipe Hees and Henrique Choer Moraes, "Breaking the BIT mould: Brazil's pioneering approach to investment agreements", AJIL Unbound, Blog of the American Journal of International Law, 2018 (forthcoming).

[2] Carlos Marcio Bicalho Cozendey and Pedro Mendonça Cavalcante, *Novas Perspectivas para Acordos Internacionais de Investimentos – o Acordo de Cooperação e Facilitação de Investimentos (ACFI)*, Cadernos de Política Exterior, Brasília, v. 1, n. 2, out. 2015, p. 89.

[3] The full English version of the Brazilian Federal Constitution of 1988 is available at: http://www.stf.jus.br/repositorio/cms/portalStfInternacional/portalStfSobreCorte_en_us/anexo/Constitution_2013.pdf (visited on March 21, 2018).

[4] Vivian Daniele Rocha Gabriel, *A proteção jurídica dos investimentos brasileiros no exterior* (São Paulo, Lex Editora, 2017).

[5] See, for example, BRAZIL-NETHERLANDS BIT, Article 6. Available at: http://investmentpolicyhub.unctad.org/Download/TreatyFile/510 (visited on March 27, 2018).

[6] Available at: http://unctad.org/en/PublicationsLibrary/wir2017_en.pdf.

[7] All bilateral agreements signed by Brazil can be consulted at: https://concordia.itamaraty.gov.br.

[8] The CFIA with Peru is Chapter 2 of the bilateral Economic and Trade Expansion Agreement, available at: http://investmentpolicyhub.unctad.org/IIA/treaty/3681.

[9] Cooperation and Facilitation Agreement Protocol Intra-MERCOSUR (PCFI). Available at: http://www.sice.oas.org/Trade/MRCSRS/Decisions/DEC_003_2017_p.pdf.

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[10] See, for example: OECD, ""Indirect Expropriation" and the "Right to Regulate" in International Investment Law", OECD Working Papers on International Investment, 2004/04 (OECD Publishing). Available from http://dx.doi.org/10.1787/780155872321.

[11] Ibid, p. 23.

[12] The exclusion of portfolio investment is clear: in all CFIAs signed by Brazil, the article on definitions clearly states that investments do not include "a) shares, stocks, and other equity and debt instruments of the enterprise or another enterprise; b) loans to an enterprise; c) movable or real estate property and other property rights such as mortgages, liens or pledges; d) claims to money or to any performance under contract having a financial value; and e) the value of investment under a concession contract or administrative decision, including licenses to cultivate, extract or exploit natural resources". All CFIA texts are available at: http://investmentpolicyhub.unctad.org/IIA/CountryBits/27#iiaInnerMenu.

[13] UNCITRAL A/CN.9/WG.III/WP.142. Available at: http://www.uncitral.org/uncitral/en/commission/working_groups/3Investor_State.html.

[14] See http://www.investkorea.org/en/ik/ombusman.do.

[15] See Investor–State Disputes: Prevention and Alternatives to Arbitration, UNCTAD Series on International Investment Policies for Development, available at http://unctad.org/en/docs/diaeia200911_en.pdf.

[16] See, for example, BRAZIL-PERU CFIA, Article 2.20.

[17] Henrique Choer Moares and Facundo Perez Aznar, "The MERCOSUR Protocol on Investment Cooperation and Facilitation: regionalizing an innovative approach to investment agreements," *EJIL Talk!*, 12 September 2017. Available from https://www.ejiltalk.org/the-mercosur-protocol-on-investment-cooperation-and-facilitation-regionalizing-an-innovative-approach-to-investment-agreements/.

[18] Mercosur Protocol on Cooperation and Facilitation of Investments, Article 23.1

[19] Mercosur Protocol on Cooperation and Facilitation of Investments, Article 24

[20] BRAZIL-PERU CFIA, Article 2.21.1

[21] See, for example, BRAZIL-CHILE CFIA, Article 25.

[22] See, for example, BRAZIL-COLOMBIA CFIA, Article 23.

[23] See, for example, BRAZIL-COLOMBIA CFIA, Article 23.2.

[24] See, for example, BRAZIL-CHILE CFIA, Annex I, Article 1.2.

[25] See, for example, BRAZIL-MEXICO CFIA, Article 19.2.

[26] See, for example, BRAZIL-INDIA CFIA, Article 19.2.

[27] See, for example, BRAZIL-MEXICO CFIA, Article 19.3.

[28] See, for example, BRAZIL-PERU CFIA, Article 2.21.4.

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