



SouthViews

No. 190, 26 February 2020

www.southcentre.int

Twitter: [@South_Centre](https://twitter.com/South_Centre)

Appeal in ISDS: Appealing for the Host State? By Grace L. Estrada

Reforms to Investor-State Dispute Settlement (ISDS) are being discussed in the United Nations Commission on International Trade Law (UNCITRAL) Working Group III. One possible reform is the development of an appellate mechanism, either as part of the proposed two-tier standing investment court, or as a stand-alone appellate mechanism. From the perspective of developing countries as host states that face possible claims from investors, how appealing is an appellate mechanism in ISDS?

Des discussions sont en cours au sein du groupe de travail III de la Commission des Nations unies pour le droit commercial international (CNUDCI) en vue de réformer le mécanisme de règlement des différends entre investisseurs et États. Parmi les propositions présentées figure la possibilité d'instaurer une procédure d'appel soit devant l'instance permanente prévue pour le règlement des différends en matière d'investissements, soit devant une instance autonome. Du point de vue des pays en développement, en tant qu'États d'accueil susceptibles d'être confrontés à d'éventuelles réclamations de la part des investisseurs, la question se pose de l'attrait que peut revêtir, dans le cadre du mécanisme de règlement des différends entre investisseurs et États, l'instauration d'une telle procédure.

En el Grupo de Trabajo III de la Comisión de las Naciones Unidas para el Derecho Mercantil Internacional (CNUDMI) se está debatiendo la reforma del sistema de solución de controversias entre inversores y Estados (ISDS, del inglés Investor-State Dispute Settlement). Una posible reforma consiste en el desarrollo de un mecanismo de apelación, ya sea como parte del propuesto tribunal permanente de inversiones de dos niveles, o como un mecanismo de apelación independiente. Desde la perspectiva de los países en desarrollo como Estados receptores que pueden verse enfrentados a posibles reclamos por parte de los inversores, ¿qué tan atractivo es un mecanismo de apelación en el ISDS?

The landscape of Investor-State Dispute Settlement (ISDS) mechanism may soon see drastic changes. The United Nations Commission on International Trade Law (UNCITRAL) is providing an avenue for states and relevant organizations to discuss the introduction of reforms to ISDS mechanism. The UNCITRAL has "entrusted Working Group III with a broad mandate to work on

the possible reform of investor-State dispute settlement."¹ How the dynamic discussions in the working group will unfold is much anticipated.

As a first step, the UNCITRAL working group has identified concerns. These concerns are as follows: (1) consistency, coherence, predictability and correctness of arbitral decisions by ISDS tribunals; (2) arbitrators/decision makers; and (3) costs and duration.² To address these concerns, reforms to ISDS have been proposed and will be considered in the upcoming sessions.

One possible reform is the development of an appellate mechanism, either as part of the proposed two-tier standing investment court, or as a stand-alone appellate mechanism.

From the perspective of developing countries as host states that face possible claims from investors, how appealing is an appellate mechanism in ISDS? What impact does having such a mechanism have on the host state?



Reforms to ISDS are being discussed in UNCITRAL Working Group III. (Photo credit: UN Photo by Manuel Elias)

Structure

Stand-alone Appellate Mechanism

The stand-alone appellate mechanism is envisioned as being a body tasked with the review of awards and decisions made by an arbitral tribunal, or possibly, even a regional investment court, international commercial court, or domestic court.

¹ Official Records of the General Assembly, Seventy-second Session, Supplement No. 17 (A/72/17), paras. 263 and 264, pp. 46-47.

² Possible reform of investor-State dispute settlement (ISDS), 36th session (A/CN.9/WG.III/WP.149), p. 3.

Standing Multilateral Investment Court³

A radical reform to ISDS is the establishment of a two-tier multilateral investment court, composed of a first instance court and an appellate court.

The appellate tribunal would hear cases elevated from the first instance court. As proposed to UNCITRAL by the European Union (EU) and its members, the grounds for appeal would include error of law, manifest error in appreciation of facts, and would exclude a new review of facts.⁴

The mechanism would include a provision to ensure that the possibility of appeal is not abused. This could include “requiring security for cost to be paid.”⁵

The framework for the appellate mechanism is still to be determined, but under both, the host state may appeal.

Matters Subject of Appeal

Appeal is seen as a means to rectify errors of law and appreciation of facts, and thus, seen as directly addressing the concern on consistency, coherence, predictability and correctness of decisions.⁶

The possible structure of the appellate mechanism is summarized by the UNCITRAL Working Group III Secretariat in a document entitled “Possible reform of investor-State dispute settlement (ISDS),” as seen in the table⁷ below:

<i>Possible reforms</i>	<i>Elements of the reforms - Link to other reform options</i>	<i>Main implications</i>	<i>Concerns addressed</i>
<p>(i) Stand-alone review or appellate mechanism</p> <p>Mentioned in:</p> <p><i>A/CN.9/WG.III/WP.159/Add.1, submission from the European Union and its Member States (Appellate body, see also below A(iii))</i></p> <p><i>A/CN.9/WG.III/WP.161, submission from the Government of Morocco (Prior scrutiny of awards and standing appellate mechanism)</i></p> <p><i>A/CN.9/WG.III/WP.163,</i></p>	<p>Review of decisions</p> <p>Scrutiny system for awards prior to issuance</p> <p>Streamlined procedure for post-award actions such as interpretation, revision and annulment</p> <hr/> <p>Appellate mechanism</p> <p>Development of an appellate mechanism, possibly tasked with a review of awards and decisions made by:</p>	<p>Review of decisions</p> <p>Setting up of a mechanism for review of ISDS tribunals decisions prior to issuance</p> <hr/> <p>Appellate mechanism</p> <p>The relationship between an appellate mechanism and the ICSID Convention, which excludes any appeal or other remedy, except for those provided for in the Convention</p>	<p>Review of decisions</p> <p>Absence of, or limited mechanisms in many existing treaties to address inconsistency and incorrectness of decisions</p> <hr/> <p>Appellate mechanism</p> <p>Absence of, or limited mechanisms in many existing treaties to address inconsistency and incorrectness of</p>

³ It is worth noting that this proposal is similar to the Investment Court System (ICS) under the Comprehensive Economic and Trade Agreement (CETA) between the European Union and Canada.

⁴ Submission from the European Union and its Member States to UNCITRAL Working Group III (A/CN.9/WG.III/WP.159/Add.1), para. 3.3, p. 4.

⁵ *Ibid.*

⁶ Submission from the European Union and its Member States to UNCITRAL Working Group III (A/CN.9/WG.III/WP.159/Add.1), para. 3, p. 4.

⁷ <https://undocs.org/en/A/CN.9/WG.III/WP.166/Add.1>, p. 3.

<p><i>submission from the Governments of Chile, Israel and Japan</i> (Treaty-specific appellate review mechanism)</p> <p>A/CN.9/WG.III/WP.175, <i>submission from the Government of Ecuador</i> (Standing review and appellate mechanism)</p> <p>A/CN.9/WG.III/WP.177, <i>submission from the Government of China</i> (Stand-alone appellate mechanism)</p>	<ul style="list-style-type: none"> - Arbitral tribunals - International investment court - Regional investment court - International commercial courts - Domestic courts in case of denial of justice <p>Determination of the framework within which it will be developed; it can be implemented jointly with any other reform options</p>	<p>itself (Article 53) would deserve careful consideration</p> <p>The impact on the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958) should also be addressed</p>	<p>decisions</p>
<p>(iii) Standing first instance and appeal investment court, with full-time judges</p> <p>Mentioned in:</p> <p>A/CN.9/WG.III/WP.159/Add.1, <i>submission from the European Union and its Member States</i></p> <p>Also discussed in:</p> <p>A/CN.9/WG.III/WP.176, <i>submission from the Government of South Africa</i></p> <p>A/CN.9/WG.III/WP.179, <i>submission from the Government of the Republic of Korea</i></p> <p>A/CN.9/WG.III/WP.180, <i>submission from the Government of Bahrain</i></p>	<p>Setting-up of a multilateral investment court, which would require preparing a statute to determine its functioning</p> <p>This reform option would cover, and possibly work in conjunction with, other reform options. The option may make a number of other options for reform redundant</p>	<p>The co-existence or articulation with the existing ISDS regime as well as with regional investment courts would need to be considered</p>	<p>Limits of the current mechanisms to address inconsistency and incorrectness of decisions</p> <p>Concerns addressed in relation to arbitrators and decision-makers</p> <p>Cost and duration</p>

Appeal and the Concern on Consistency, Coherence, Predictability and Correctness of Decisions

The concern on consistency, coherence, predictability and correctness of arbitral decisions by tribunals was explained as having "divergent interpretations of substantive standards; divergent interpretations relating to jurisdiction and admissibility; and procedural inconsistency."⁸ In elucidating on this, illustrations were given, such as different interpretations on the substantive provisions of fair and equitable treatment, umbrella clause, essential security provisions/necessity doctrine, as well as different interpretations on jurisdiction and admissibility and the application of inconsistent procedure.⁹

⁸ Possible reform of investor-State dispute settlement (ISDS), 36th session (A/CN.9/WG.III/WP.149), para. 9, p. 3.

⁹ Possible reform of investor-State dispute settlement (ISDS): Consistency and related matters, 36th session (A/CN.9/WG.III/WP.150), paras. 16-18, pp. 5-11.

Investment agreements rarely provide clear definitions of these substantive provisions, leaving the arbitrators to interpret them. Absent an understanding of the host state's laws and regulations, arbitrators have been known to "have interpreted issues of domestic law from a commercial rather than public policy perspective."¹⁰

The oft-cited International Centre for Settlement of Investment Disputes (ICSID) cases of *SGS v. Philippines*¹¹ and *SGS v. Pakistan*¹² are a glaring illustration of inconsistent and conflicting interpretations of a similar provision. The investor in these cases is a Swiss corporation, which filed a claim under Switzerland's respective bilateral investment treaties (BITs) with the Philippines and Pakistan. The provision under consideration was the umbrella clause¹³ in the relevant BITs. Both the Philippines and Pakistan stated that the respective tribunals did not have jurisdiction over the claim of SGS, because the relationship between the parties is based on a contract, the dispute is based on the termination of the contract, and, thus, not covered by the BIT. The pertinent phrase of the provision is "disputes with respect to investments." The tribunal in *SGS v. Philippines* interpreted this phrase as applicable to the contract between the parties, because it comes under the BIT's umbrella clause. On the other hand, the tribunal in *SGS v. Pakistan* "did not find that the umbrella clause in the Switzerland–Pakistan BIT would place the state's contractual and domestic law obligations under the treaty arbitration mechanism."¹⁴ The contrasting interpretations such as in these cases make arbitration unstable and unreliable. As observed, "[t]he two conflicting interpretations in *SGS v. Pakistan* and *SGS v. Philippines* on this issue create significant uncertainty regarding hundreds of broad dispute resolution clauses in BITs and their impacts upon forum selection clauses in an unknown, but likely extensive, number of investor–state contracts."¹⁵

Another identified dire consequence of inconsistent and divergent interpretations by the arbitral tribunal is restricting the state's regulatory power to serve public interest. In other words, "claims or threats by investors to bring forward a case against a particular state have been used as ways to prevent new legislation and other measures from being adopted or applied, thus effectuating a 'chilling effect' on the regulatory process."¹⁶ Thus, a state regulation made for legitimate public policy could be limited or set aside.

The working group has expressed the importance of considering a reform regarding this concern, in light of the intention to bring consistency and coherence to ISDS decisions as such would "support the rule of law, enhance confidence in the stability of the investment environment and further bring legitimacy to the regime."¹⁷

¹⁰ Kinda Mohamadieh, "The Future of Investor-State Dispute Settlement Deliberated at UNCITRAL: Unveiling a Dichotomy between Reforming and Consolidating the Current Regime," South Centre Investment Policy Brief No. 16 (March 2019), p. 2.

¹¹ *SGS Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6 (Decision on Objections to Jurisdiction and Separate Declaration)

¹² *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13 (Decision on Objections to Jurisdiction)

¹³ Under an 'umbrella clause', arbitrations can involve not only obligations contained in the investment treaties themselves but also those in investor-state contracts as well as any dispute relating to investments.

¹⁴ *SGS v. Pakistan*, International Investment Law and Sustainable Development [18 October 2018] (www.iisd.org/itn/2018/10/18/sgs-v-pakistan)

¹⁵ *SGS v. Philippines*, International Investment Law and Sustainable Development [18 October 2018] (www.iisd.org/itn/2018/10/18/sgs-v-philippines)

¹⁶ Mohamadieh, *supra*, p. 2.

¹⁷ Possible reform of investor-State dispute settlement (ISDS), 36th session (A/CN.9/WG.III/WP.149), *supra*, para. 26, p. 7.

Will an appellate mechanism satisfactorily address these concerns?

The issues for appeal would be error of law or manifest error in appreciation of facts. The incorporation of an appellate mechanism seeks to address the concern on inconsistent decisions of the arbitral tribunal, by allowing a higher tribunal to rectify the errors of the first instance court. An appellate mechanism would result in "reducing inconsistencies and hence further predictability."¹⁸ Likewise, it has been practiced by arbitral tribunals to refer to past decisions, and so, "one can argue that an appeal mechanism aligned with this trend of arbitral tribunals referring to previous decisions will allow ISDS to achieve a more 'consistent body of decisions'."¹⁹

The value of an appellate mechanism would be the strengthening of the credibility of the ISDS system if it produces consistent, predictable and correct decisions.

Nonetheless, the host state has to be mindful of the obligations and concessions it made under different international investment agreements (IIAs). "A disperse system composed of some 3,000 different Bilateral Investment Treaties ("BIT's") has generated beliefs that some degree of inconsistency will be inevitable. In fact, it might be difficult to resolve similar issues in a similar way when the reality is that BIT's are negotiated by different States, in different circumstances and with different interests and arbitral tribunals are bound to make their decisions based on the respective treaty and on a case-by-case basis."²⁰ A host state that has a higher interest of attracting foreign investors from one particular state may give such state more favorable concessions and obligations than other states as treaty partners.

In other words, the basis of a claim in ISDS is always the applicable IIA. The tribunal would always refer to its provisions, and interpret them in the manner presented by the parties, one of which is the party to the IIA. Thus, with different treaties as bases of claims, despite similarity in facts, issues and obligations subject of the dispute, there would always be differences and inconsistencies. This is a consequence of the 'fragmented' state of the international investment system. Moreover, in other cases the arbitration tribunals have decided differently even when provisions in the treaties were exactly the same, particularly in the case of parallel proceedings.

Appeal and the Concern on Cost and Duration

On its face, it is logical that appeal, being an additional layer to dispute settlement, means additional cost and longer period to resolve the dispute. Increased costs for the proceedings because of the features of "appeal and the participation of a potentially large number of third party interveners, not to mention *amici curiae*, seems very real and is not, or only barely, considered in the [investment court system] proposal."²¹ The effect of increased costs would be burdensome on the respondent state, and reform would be "insufficient to increase the access

¹⁸ Catherine Li, "The EU's Proposal Regarding the Establishment of the Investment Court System and the Response from Asia," *Journal of World Trade* 52, no. 6 (2018), pp. 948-949.

¹⁹ Aceris Law LLC, "Appellate Mechanism for ISDS: Inconsistency and Unpredictability of Arbitration Awards", 30 September 2018. Available from <https://www.acerislaw.com/appellate-mechanisms-for-isds-inconsistency-unpredictability-of-arbitration-awards>.

²⁰ *Ibid.*

²¹ Freya Baetens, "The European Union's Proposed Investment Court System: Addressing Criticisms of Investor-State Arbitration While Raising New Challenges," *Legal Issues of Economic Integration* 43, no. 4 (2016): 367-384, 380.

of [small and medium enterprises]²² and “facilitate the adjudication of smaller claims.”²³

As appeal is available, it is foreseen that the losing party will appeal as a matter of course. The appeal mechanism is seen as prolonging the period for the resolution of a dispute.

This doomsday scenario, though, may not happen. Taking cue from the World Trade Organization (WTO) Dispute Settlement Understanding (DSU), where disputes may be appealed, such prolonged dispute resolution may be temporary. “The WTO experience demonstrates that this may indeed be the case in five years, but that as soon as a ‘predictable’ jurisprudence emerges, the number of appeals decreases.”²⁴ The ultimate objective of providing an appeal mechanism is to provide consistent decisions. If the appeal mechanism of the proposed permanent investment court mirrors WTO history, the advantage of an appellate mechanism would be felt in the long run.²⁵ Resort to appeal may eventually lessen, when there is a richer compilation of consistent decisions.

Relationship of Appellate Mechanism to ICSID and New York Convention

The International Centre for Settlement of Investment Disputes, established pursuant to the Convention on the Settlement of Investment Disputes between States and Nationals of other States (ICSID Convention), is an ISDS forum in most IIAs. Article 53 of the Convention specifically states that awards “shall not be subject to any appeal or to any other remedy.”

Thus, appealing arbitral awards under the ICSID Convention may not be possible, even if provided under the ISDS provision of the governing treaty, or under the agreement establishing such an appellate mechanism. Unless the ICSID Convention is amended to accommodate appeal, awards are final.

With respect to enforcement of awards under the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention), there may be a need to connect the awards made in the appellate mechanism, with the New York Convention. There may be a need to revisit the application of the New York Convention, and the definition of “arbitral awards,” in relation to its Article V and the domestic law of the territory of the court where award is sought to be recognized and enforced.

Impact upon the Host State

The host state that faces possible arbitration would have to balance its interests. On one hand, having an appellate mechanism in ISDS is anticipated to produce consistent, predictable decisions that will eventually yield fewer errors. In the long run, and ideally, it will lead to less and less disputes.

Yet, the more immediate and practical concerns on cost and duration are burdens that the host states bear. As aptly observed, “the principle of finality of arbitral awards has been one of the most attractive features of international investment arbitration, because it saved time and

²² *Ibid.*

²³ *Ibid.*

²⁴ *Ibid.*

²⁵ Given the wide range of investment related issues and plurality of agreements under which ISDS cases can be brought, a strong corpus of consistent decisions might take longer to develop than in WTO. Even in the WTO context, despite having over 20 years of jurisprudence, about 77% of all panel reports were still appealed in the last 5 years.

money."²⁶ An appellate mechanism would necessarily lengthen the proceedings and incur additional costs for the parties.

The host state may also reconsider its policies on ISDS, such as resorting to the ICSID Convention where there is no possibility of appeal, application of the New York Convention, and generally, reviewing its existing IIAs to accommodate an appellate mechanism, or a standing two-tier investment court.

Alternative to Appeal

To the end of addressing the concerns on consistency, coherence, predictability and correctness of decision, the establishment of an appellate mechanism may not be the only answer.²⁷

The states parties to IIAs have used approaches to ISDS provisions that manifest control over interpretation of treaty provisions, and minimal resort to ISDS. Some IIAs have provisions on joint interpretation by the Parties, or application of ISDS to only certain treaty breaches.

Joint Interpretation by Parties

Joint interpretation is a provision found in some IIAs, wherein the State party to the dispute, and the home State of the disputing investor, adopt binding interpretations of the treaty obligations. Joint interpretation made by the Parties to the IIA provides clarity on the interpretation and application of treaty obligations, restricts its interpretation, and is meant to bind the tribunal. By way of example, the Association of Southeast Asian Nations (ASEAN)-India Investment Agreement has a provision on joint interpretation "of any provision of this Agreement that is in issue in a dispute."²⁸

The objective of having a provision on joint interpretation is for the Parties to bind the tribunal on the definition based on the Parties' understanding and intention on treaty obligations, such as fair and equitable treatment. In this manner, the tribunal is not given a wide discretion in its own interpretation and application to the set of facts. More importantly, joint interpretation of treaty obligations is recognized as a crucial exercise wherein "states can help provide this clarity, and, in doing so, control the scope of their potential liability (and litigation costs) under their existing, long-lasting investment treaties."²⁹

Application of ISDS only to Certain Breaches of Treaty Obligation

In "new generation" IIAs, there are provisions that ISDS would apply only to certain treaty breaches. By limiting the applicability of ISDS, the States limit the scope of jurisdiction of the arbitral tribunal or court. In doing so, the States not only limit opportunity for investors to make

²⁶J. Chaisse and Y. Renouf, "Investor-State Dispute Settlement", in *Potential Benefits of an Australia-EU Free Trade Agreement: Key Issues and Options*, J. Drake-Brockman & P. Messerlin, eds. (South Australia, University of Adelaide Press, 2018), p. 303. Available from www.jstor.org/bibliopass.unito.it/stable/j.ctv9hj94m.23. Accessed 4 July 2019.

²⁷ Other options include preventive mechanisms (e.g. good offices, ombudsman), state-to-state dispute resolution and joint committees.

²⁸Article 20(19).

²⁹Lise Johnson and Merim Razbaeva, "State Control over Interpretation of Investment Treaties" (Vale Columbia Center on Sustainable International Investment, April 2014). Available from http://ccsi.columbia.edu/files/2014/04/State_control_over_treaty_interpretation_FINAL-April-5_2014.pdf. Accessed 4 July 2019.

a claim under ISDS, they also preserve their right to regulate.

Conclusion

The attractiveness of having an appellate mechanism or a standing investment court depends on the priorities and considerations of the party to ISDS cases that will be heavily hit, i.e. the host state. For the host state, is the possibility of consistent and correct decisions in the long run worth the costlier and longer proceedings? Would the host state make the appellate mechanism work with existing ISDS platforms? In transitioning to a standing investment court, or having a stand-alone appellate mechanism in its ISDS, what adjustments to its domestic laws, and agreements would the host state make? Or would alternative options work for the host state?

The proposed reform, albeit a radical one, has its appeal. The host states need to carefully take into account if its appeal outweighs other considerations.

Author: Grace L. Estrada is a State Counsel of the Philippine Department of Justice. E-mail: glestrada@gmail.com

*** The views contained in this article are attributable to the author and do not represent the institutional views of the South Centre or its Member States.**

SOUTHVIEWS is a service of the South Centre providing opinions and analysis of topical issues from a South perspective.

To view other articles in SouthViews, please [click here](#).

To see the previous version of SouthViews, please [click here](#).

For more information, please contact Anna Bernardo of the South Centre: Email bernardo@southcentre.int, or telephone +41 22 791 80 50.

Copyright © 2020 South Centre, All rights reserved.