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INVESTOR-STATE ARBITRATION BETWEEN DEVELOPED DEMOCRATIC COUNTRIES

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TABLE OF CONTENTS

- iv** About the Investor-State Arbitration Project
- iv** About the Author
- v** Acronyms
- 1** Introduction to the Issues
- 7** Criticisms Levelled against ISA and the Answers That May Be Given
- 23** Proposed Solutions and Analysis of the Challenges Facing the Effort to Reform ISA
- 33** The Way Forward?
- 34** About CIGI
- 34** CIGI Masthead

ABOUT THE INVESTOR-STATE ARBITRATION PROJECT

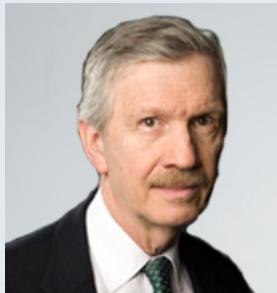
Launched in November 2014, this project is addressing a central policy issue of contemporary international investment protection law: is investor-state arbitration (ISA) suitable between developed liberal democratic countries?

The project will seek to establish how many agreements exist or are planned between economically developed liberal democracies. It will review legal and policy reactions to investor-state arbitrations taking place within these countries and summarize the substantive grounds upon which claims are being made and their impact on public policy making by governments.

The project will review, critically assess and critique arguments made in favour and against the growing use of ISA — paying particular attention to Canada, the European Union, Japan, Korea, the United States and Australia, where governments, legal establishments and civil society groups have come out against ISA. The project will examine the arguments that investor-state disputes are best left to the national courts in the subject jurisdiction. It will also examine whether domestic law in the countries examined gives the foreign investor rights of action before the domestic courts against the government equivalent to those provided by contemporary investment protection agreements.

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Armand's current research interest is the law of international economic integration. He has prepared books, articles and studies in English and French on international trade law and on Canadian and comparative constitutional and international law. He has served on World Trade Organization and North American Free Trade Agreement dispute settlement tribunals, as well as public and private arbitration tribunals. He was made a Member of the Order of Canada in December 2007.

ACRONYMS

AB	Appellate Body
AUSFTA	Australia-United States Free Trade Agreement
BIT	bilateral investment treaty
CETA	Comprehensive Economic Trade Agreement
CIETAC	China International Economic and Trade Arbitration Committee
CJEU	Court of Justice of the European Union
DSU	Dispute Settlement Understanding
ECHR	European Court of Human Rights
FET	fair and equitable treatment
FIPA	Foreign Investment Protection Agreement
FTA	free trade agreement
GATT	General Agreement on Tariffs and Trade
ICC	International Chamber of Commerce
ICJ	International Court of Justice
ICSID	International Centre for Settlement of Investment Disputes
IIA	international investment agreement
IISD	International Institute for Sustainable Development
ISA	investor-state arbitration
ISDS	investor-state dispute settlement
LCIA	London Court of International Arbitration
MAI	Multilateral Agreement on Investment
MFN	most-favoured nation
MNE	multinational enterprise
NAFTA	North American Free Trade Agreement
NT	national treatment
OECD	Organisation for Economic Co-operation and Development
RTA	regional trade agreement
TPP	Trans-Pacific Partnership
TTIP	Transatlantic Trade and Investment Partnership
TRIMS	Trade Related Investment Measures
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
WTO	World Trade Organization

*Facilis descensus Averno;
noctes atque dies patet atri ianua Ditis;
sed revocare gradum superasque evadere ad auras,
hoc opus, hic labor est.*

Virgil, *The Aeneid*, Book 6, Line 126

*The gates of hell are open night and day;
Smooth the descent, and easy is the way:
But to return, and view the cheerful skies,
In this the task and mighty labor lies.*

Translation by John Dryden, 1697

INTRODUCTION TO THE ISSUES

Investor-state arbitration (ISA)¹ is a treaty-based form of arbitration by which a state agrees, in advance, to be the object of a claim in arbitration by a private investor who claims to have suffered financial loss as a result of violation of one or more standards of treatment set out in the treaty. These treaties usually take the form of bilateral investment treaties (BITs),² but, in recent decades, many provisions for foreign investment protection are to be found in the investment chapters of regional trade agreements (RTAs)³ and latterly in so-called mega-regional trade agreements⁴ between major countries or blocs of countries, such as the Comprehensive Economic and Trade Agreement (CETA) between Canada and the European Union,⁵ the Transatlantic Trade and Investment Partnership (TTIP)⁶ and the Trans-Pacific Partnership (TPP).⁷

BITs and RTAs with investment chapters have come to represent a global phenomenon. The United Nations Conference on Trade and Development (UNCTAD) calculates that there are more than 3,200 international investment agreements (IIAs).⁸ It is more difficult to obtain an accurate number of those treaties that contain ISA, but they comprise the great majority of those signed since the negotiation of the first modern BIT between Germany and Pakistan in 1959.⁹ The economic impact of ISA, which came into widespread use only in the 1970s, is much debated, but its proponents consider that it should be seen as an essential guarantee of respect of the standards set out in BITs. They argue that it is key to protecting the interests of foreign investors and foreign investments against the possible failure of the host country to respect treaty standards, and that this protection encourages the flow of foreign investment.¹⁰

1 Also known as investor-state dispute settlement (ISDS), an expression that can confusingly embrace both arbitration and intergovernmental dispute settlement.

2 See e.g. Section C of the Canadian Model Foreign Investment Protection Agreement (FIPA) (*Agreement Between Canada and _____ for the Promotion and Protection of Investments*, 2004). Such provisions are provided under most BITs.

3 For a breakdown of the sources of consent invoked to establish International Centre for Settlement of Investment Disputes (ICSID) jurisdiction in cases registered in 2014, see ICSID, *The ICSID Caseload: Statistics*, Issue 2015-1 at 23, online: ICSID <[https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%202015-1%20\(English\)%20\(2\)_Redacted.pdf](https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%202015-1%20(English)%20(2)_Redacted.pdf)>.

4 It is noteworthy that most mega-regionals are still being negotiated.

5 For up-to-date information concerning CETA, see European Commission, “Comprehensive Economic and Trade Agreement (CETA)”, online: <ec.europa.eu/trade/policy/in-focus/ceta/>.

6 For up-to-date information concerning the TTIP, see European Commission, “The Transatlantic Trade and Investment Partnership (TTIP)”, online: <ec.europa.eu/trade/policy/in-focus/ttip/>.

7 For up-to-date information concerning the TPP, see Office of the United States Trade Representative, “Trans-Pacific Partnership (TPP)”, online: <www.usit.gov/tpp>.

8 UNCTAD, *World Investment Report 2015: Reforming International Investment Governance* (Geneva: United Nations, 2015) at 106, online: <unctad.org/en/PublicationsLibrary/wir2015_en.pdf> (“The conclusion in 2014 of 31 international investment agreements (IIAs)—18 bilateral investment treaties (BITs) and 13 ‘other IIAs’—brought the total number of IIAs to 3,271 (2,926 BITs and 345 ‘other IIAs’) by year-end”).

9 *Treaty for the Promotion and Protection of Investments*, Pakistan and Federal Republic of Germany, 25 November 1959, 457 UNTS 6575, online: <www.iisd.org/pdf/2006/investment_pakistan_germany.pdf>. This treaty did not, in fact, contain ISA provisions.

10 See Rudolf Dolzer & Christoph Schreuer, *Principles of International Investment Law* (Oxford: Oxford University Press, 2008) at 214–15.

The basic standards set out in BITs have remained relatively constant since 1959. They include, principally, the standards of most-favoured nation (MFN) and national treatment (NT), a guarantee of “fair and equitable treatment” (FET) and often also “full protection and security.” They also include a prohibition against certain forms of performance requirements binding the foreign investor to perform specific obligations as a condition precedent to allowing the investment.¹¹ Finally, virtually all BITs repeat the public international law prohibition against expropriation of foreign-owned assets unless for a public purpose and accompanied by prompt and effective compensation. These key protections are included in most BITs, but they may be worded in different ways and there is no uniform format for all BITs. Other protections, such as the determination of whether the standards are applied only after the investment is allowed or whether it applies also to the pre-investment phase, may be added according to the policies of the negotiators. What has changed over time is the length and complexity of the BITs. The early so-called gold standard BITs concluded by European governments are seldom more than 10 pages in length and are limited to setting out basic general principles. More recently, for a variety of reasons that will be discussed below, model BITs have become much more extensive, as far as their substantive and procedural provisions are concerned, and set out the principles in much greater detail. They also tend to set out a wide range of exceptions, interpretations and detailed provisions designed to protect the exercise of authority by contracting governments, with the aim of protecting public policies regulating commercial transactions, consumer protection, environmental and health standards and the protection of human rights.¹²

This new approach to drafting has been particularly evident in the context of RTAs subsequent to the conclusion of NAFTA in 1994, and has characterized virtually all RTAs with investment chapters concluded in recent years by the European Union, Canada, the United States and Japan.¹³ But the new approach has by no means been restricted to RTAs and has come to characterize many recently concluded BITs of Canada,¹⁴ the United States¹⁵ and Japan,¹⁶ and has clearly been adopted by the European Union since it acquired competence over foreign direct investment matters in 2009.¹⁷ Some states have adopted more radical approaches. Recently, South Africa suggested it would withdraw from many BITs¹⁸ while Indonesia and India have issued new model BITs for the future¹⁹ and UNCTAD

11 It is noteworthy, however, that the prohibition of performance requirements, which can be described as an innovation of the *North American Free Trade Agreement* (NAFTA), is encountered less often in investment agreements than the other traditional standards of protection.

12 See e.g. Canadian Model FIPA (2004), arts 10, 11, 16 and 17; US Model BIT (2012), arts 12, 13, 18, 20 and 21; Norway Model BIT (2007), arts 24, 25, 26 and 28.

13 See e.g. CETA, *supra* note 5; the TPP’s (*supra* note 7) leaked investment chapter; the investment chapter (Chapter 8) of the *Free Trade Agreement Between Canada and Korea*, 22 September 2014, online: <investmentpolicyhub.unctad.org/IIA/country/35/treaty/3486>; the investment chapter (Chapter 10) of the *Free Trade Agreement Between Canada and Honduras*, 5 November 2013 (entered into force 1 October 2014), online: <investmentpolicyhub.unctad.org/IIA/country/35/treaty/3403>; the investment chapter (Chapter 10) of the *Free Trade Agreement Between the United States and Panama*, 28 June 2007 (entered into force 31 October 2012), online: <investmentpolicyhub.unctad.org/IIA/country/223/treaty/3219>; the investment chapter (Chapter 14) of the *Agreement Between Australia and Japan for an Economic Partnership*, 8 July 2014, online: <investmentpolicyhub.unctad.org/IIA/country/105/treaty/3487>.

14 See e.g. Canada-China BIT (2012), art 33, Benin-Canada BIT (2013), arts 15 and 20 or the Canada-Mali BIT (2014), arts 15 and 17.

15 See e.g. arts 12, 13, 18, 20 and 21 of the Rwanda-United States BIT (2008).

16 See e.g. arts 7, 16, 18, 19 and 21 of the Japan-Korea BIT (2002) or art 25 of the Japan-Ukraine BIT (2015).

17 This approach is most apparent in the recently signed CETA. See also European Commission, *Towards a comprehensive European international investment policy*, Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, Brussels (7 July 2010), COM (2010) 343 final, online: <trade.ec.europa.eu/doclib/html/147884.htm> and Council of the European Union, *Conclusions on a comprehensive European international investment policy*, 3041st Foreign Affairs Council meeting, Luxembourg (25 October 2010), online: <www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/EN/foraff/117328.pdf>.

18 South Africa is indeed engaged in the process of terminating several bilateral investment treaties with European countries. For instance, it terminated its BIT with the Belgian-Luxembourg Economic Union, Germany, the Netherlands or Spain. See “International Investment Agreements Navigator”, online: <investmentpolicyhub.unctad.org/IIA> and IISD, “News in Brief”, *Investment Treaty News* (30 October 2012), online: <www.iisd.org/itn/2012/10/30/news-in-brief-9>.

19 See e.g. Ben Bland, “Indonesia to terminate more than 60 bilateral investment treaties”, *The Financial Times* (26 March 2014), online: <www.ft.com/cms/s/0/3755c1b2-b4c2-11e3-af92-00144feabcd0.html#axzz3PPXqDH1>. Concerning India, see generally Prabhash Ranjan, “India and Bilateral Investment Treaties: A Changing Landscape” (2014) 29:2 ICSID Review 419.

reports that no less than 45 states are reviewing their BITs. Venezuela, Bolivia and Ecuador have taken the step of withdrawing from the ICSID Convention.²⁰

BITs were originally designed to deal with capital transfers between capital-exporting (usually First World) and capital-importing (usually Developing World) countries.²¹ Some 1,200 BITs exist between European and developing countries. But today the majority of BITs are concluded on a South-South basis. Until the fall of the Berlin Wall, it was also common for many Western countries to conclude BITs with states in the Communist Bloc.²² Very few BITs were concluded between developed democracies.²³ One early exception was the Freedom, Commerce and Navigation agreement (known as the FCN) between the United States and Italy, which became the object of the *Elettronica Sicula* decision of the International Court of Justice (ICJ).²⁴ When Canada and the United States concluded an important trade agreement in 1988, it included a groundbreaking investment chapter, but no ISA.²⁵ However, when Canada, the United States and Mexico negotiated an even more influential trade agreement (NAFTA) in 1994,²⁶ Part B of Chapter 11 dealing with investments was devoted to ISA in order to deal with problems perceived to exist in Mexico. There is reason to believe that NAFTA began the process of including ISA in the investment chapters of RTAs, which is currently playing itself out with the conclusion of mega-regional RTAs involving developed democracies as well as a variety of other countries.

The European Union constitutes a particularly interesting and complex case, in that it is made up of many of the countries that originated the practice of concluding BITs, such as Germany, France, the Netherlands and the United Kingdom. In 2009, the member states of the European Union took the important step of transferring competence over foreign direct investment to the European Union.²⁷ This is part of the Common Commercial Policy and is thus, in principle, an exclusive competence of the European Union, although some doubts remain as to the precise ambit of the competence, and the Court of Justice of the European Union (CJEU) has yet to rule on the issue.²⁸ EU member states have signed some 1,200 BITs with other states and, as a result of the adhesion of the 12 central European states in 2004 and 2006, there are now some 190 BITs between EU member states themselves.²⁹

The transfer of competence to the European Union has had the result of forcing the member states and the commission to adopt a new, specifically EU approach to negotiating BITs and investment chapters in RTAs. Some states and observers³⁰ were of the view that the European Union should continue to negotiate on the basis of the traditional “gold standard” model of the member states; however, a lively debate quickly arose in the EU Parliament as to the apprehended dangers of the traditional approach

²⁰ Pursuant to article 71 of the ICSID Convention, the Plurinational State of Bolivia notified its intention to withdraw from the ICSID Convention on 2 May 2007, which took effect on 3 November 2007. Similarly, Ecuador submitted the written notice of its withdrawal on 6 July 2009, which became effective on January 2010. Ecuador is also engaged in a global process of withdrawal from several IIAs. (“In 2008, Ecuador terminated nine BITs with Cuba, the Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, Romania and Uruguay. Other denounced BITs include those between El Salvador and Nicaragua, and the Netherlands and the Bolivarian Republic of Venezuela. In 2010, Ecuador’s Constitutional Court declared arbitration provisions of six more BITs (China, Finland [since then the Ecuador-Finland has been terminated], Germany, the UK, Venezuela and United States) to be inconsistent with the country’s Constitution.” [UNCTAD, “Denunciation of the ICSID Convention and BITs: Impact on Investor-State Claims”, (December 2010) IIA Issues Note No 2, UN Doc UNCTAD/WEB/DIAE/IA/2010/6]. Finally, the World Bank received the Bolivarian Republic of Venezuela’s written notice of denunciation of the ICSID Convention on 24 January 2012, which took effect on 25 July 2012. Venezuela thus became the third state to withdraw from the ICSID Convention.

²¹ See Dolzer & Schreuer, *supra* note 10 at 17ff. See also UNCTAD, *World Investment Report 2014: Investing in the SDGs: An Action Plan* (Geneva: United Nations, 2014) at 123, online: <unctad.org/en/PublicationsLibrary/wir2014_en.pdf>.

²² In particular, before NAFTA, Canada mainly entered into BITs with the USSR and several countries of the Soviet Bloc.

²³ In this regard, UNCTAD’s *2014 World Investment Report* (*supra* note 21) indicates that by the end of 2013 only nine percent of BITs were North-North. Seventy-seven percent of those BITs are entered into between members of the European Union.

²⁴ *Case Concerning Elettronica Sicula SpA (ELSI) (US v Italy)*, [1989] ICJ Rep 15; *Italy-United States Treaty of Friendship, Commerce and Navigation between the United States and Italy*, 2 February 1948, 79 UNTS 171, TIAS 1965 (entered into force 26 July 1949).

²⁵ See the *Canada-United States Free Trade Agreement* (1988), online: <www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/cusfta-e.pdf>.

²⁶ NAFTA, 11 December 1992, 32 ILM 289 at 605 (entered into force 1 January 1994).

²⁷ See the *Treaty on the Functioning of the European Union* (2008 OJ C 115/47), arts 3(1)(e), 206 and 207 [TFEU].

²⁸ In this regard, the commission requested in October 2014 an opinion of the CJEU on the competence to sign and ratify the EU-Singapore Free Trade Agreement. See European Commission, Press Release, “Singapore: The Commission to Request a Court of Justice Opinion on the Trade Deal” (30 October 2014), online: <europa.eu/rapid/press-release_IP-14-1235_en.htm>.

²⁹ See also on ISA proceedings involving European member states: ICSID, *The ICSID Caseload: Statistics (Special Focus: European Union)*, online: <<https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/Stats%20EU%20Special%20Issue%20-%20Eng.pdf>>.

³⁰ On the “gold standard” model, also known as the “Dutch gold standard,” see e.g. Nikos Lavranos, “The new EU Investment Treaties: Convergence towards the NAFTA model as the new Plurilateral Model BIT text?” (29 March 2013), online: <papers.ssrn.com/sol3/papers.cfm?abstract_id=2241455> and Gina Vetere & Marney Cheek, “A Critical Opportunity to Promote Gold Standard Investment Protections” (24 June 2014), online: <www.globalpolicywatch.com/2014/06/the-transatlantic-trade-and-investment-partnership-a-critical-opportunity-for-securing-gold-standard-investment-protections/>.

and many parliamentarians, inspired by the experience of Canada, the United States and Mexico under NAFTA Chapter 11,³¹ argued for a new approach designed to protect the capacity of member states and the European Union to adopt regulatory measures to protect consumers, the environment, public health and human rights without fear of contestation by foreign investors under ISA. Some parliamentarians and governmental ministers in Germany and France³² have even called for the abandonment of ISA in BITs. As a result of these debates, the commission has adopted an approach based on public policy protection and broad exceptions in its first trade and investment negotiations with Canada³³ and Singapore,³⁴ and is apparently taking the same approach with India and the United States. This latter negotiation has elicited a particularly strident debate over ISA, with many calling for the abandonment of recourse to ISA in the future TTIP.³⁵

The recent debate in the European Union and some of its member states seems to reflect the fact that an increasing number of BITs and RTA investment chapters are being concluded between developed democracies and, as a direct result, the governments of these democracies have been placed in the uncomfortable and unexpected position of being sued by foreign investors. During the early years, when Germany, France, the United Kingdom, the Netherlands and others were concluding BITs with developing countries, or even during the 1990s, when UNCTAD was encouraging developing countries to sign BITs with capital-exporting countries as part of the Washington Consensus approach to international development,³⁶ there was little, if any, controversy, and certainly none in developed democracies. The BITs were adopted in the developed world virtually without comment and no question was raised publicly or in national parliaments concerning the propriety of ISA as a means of guaranteeing respect for investment treaty commitments.

The first significant change in this pattern occurred in 1994 with the entry into force of NAFTA, a treaty binding two developed democracies with a third party that was a developing democracy. The American and Canadian negotiators apparently considered³⁷ it necessary to include ISA in NAFTA to ensure that Mexico respect its obligations vis-à-vis foreign investments, and apparently there was considerable surprise when first Canada³⁸ and then the United States³⁹ were sued by investors under Part B of Chapter 11. From that point on, there has been a measure of controversy and criticism of the propriety of recourse to ISA in Canada and the United States. The critics have come particularly from the ranks of environmental non-governmental organizations and other organizations representing public

31 See the document cited *supra* in note 17.

32 It is reported that “[o]n 21 January, the [French] Secretary of State for Foreign Trade Matthias Fekl went to Berlin to meet Sigmar Gabriel, the [German] Minister of Economy and Matthias Machnig, the Federal Secretary for Economic Affairs. In a joint statement, the ministers of the two countries have called on the Commission and Member States to consider ‘all options changes’ of the arbitration clause in the agreement with Canada.” A foreign ministry source adds, “What is important is that for the first time the Germans agree to the link on arbitration within CETA and TTIP.” (See the Council of Canadians, “Germany and France want to reopen CETA to amend ISDS provision” (26 January 2015), online: <www.canadians.org/>). See also EurActiv, “Paris et Berlan veulent réviser l’accord EU-Canada” (26 January 2015), online: <www.euractiv.fr/> and EurActiv, “Naissance d’un front franco-allemand contre l’arbitrage dans le cadre du TTIP” (14 January 2015), online: <www.euractiv.fr/>.

33 See CETA, *supra* note 5, Chapter 10.

34 *EU-Singapore Free Trade Agreement*, text initialled on 20 September 2013, Chapter 9 (Investment), online: <trade.ec.europa.eu/doclib/press/index.cfm?id=961>.

35 See e.g. James Kilcourse, “TTIP Faces Political Hurdles on Both Sides of the Atlantic” (3 February 2014), *Institute of International and European Affairs*, online: <www.iiea.com/blogosphere/ttip-faces-political-hurdles-on-both-sides-of-the-atlantic> and Public Citizen, “Tens of Thousands of U.S. Firms Would Obtain New Powers to Launch Investor-State Attacks against European Policies via CETA and TTIP”, online: <www.citizen.org/documents/EU-ISDS-liability.pdf>. See also Commissioner Malmström, “Investment in TTIP and beyond — the path for reform: Enhancing the right to regulate and moving from current ad hoc arbitration towards an Investment Court” (5 May 2015), Concept Paper, online: <trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF>.

36 See Dolzer & Schreuer, *supra* note 10 at 79: “In the late 1980s there was a growing international consensus that economic liberalism promised more growth and innovation than economic protectionism within closed national or regional borders. A now famous paper by J. Williamson provided a list of conditions for successful economic growth, which eventually came to be known as the ‘Washington Consensus.’”

37 Guillermo Aguilar Alvarez & William W Park, “The New Face of Investment Arbitration: NAFTA Chapter 11” (2003) 28:2 *Yale Journal of International Law* 365 at 368ff.

38 For a list of NAFTA Chapter 11 arbitration involving Canada, see Foreign Affairs, Trade and Development Canada, “NAFTA – Chapter 11 – Investment: Cases Filed Against the Government of Canada”, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/dispute-settlement/gov.aspx?lang=eng>.

39 For a list of NAFTA Chapter 11 arbitration involving the United States, see US Department of State, “Cases Filed Against the United States of America”, online: <www.state.gov/s/l/c3741.htm>.

policy constituencies,⁴⁰ who have argued that it is inappropriate to allow foreign investors to challenge domestic legislation or regulatory decisions. In the United States, the *Methanex* litigation led to petitions to Congress in 2001. A second round of criticism ensued in the United States in 2015, characterized by resolutions in Congress⁴¹ and strong statements by Massachusetts Senator Elizabeth Warren.⁴² Some of the earliest and most principled criticisms have in fact come from Canadian authors such as Gus van Harten⁴³ and David Schneiderman,⁴⁴ as well as from Howard Mann of the International Institute for Sustainable Development (IISD).⁴⁵ Subsequently, Australian commentators and advocates have been very critical of recourse to ISA by Australia.⁴⁶ The high point of this movement in Australia was the refusal of Australia to include ISA in the Australia-US Free Trade Agreement.⁴⁷ At one point, it appeared that Australia would reject all recourse to ISA, but recently the Government of Australia seems to have adopted a more nuanced policy of picking and choosing the treaties in which it will include ISA.⁴⁸ The advent of negotiations involving the United States in the TPP appears to have provoked a debate in Japan over recourse to ISA.⁴⁹ Currently there is little public debate on the issue in Korea, but several years ago ISA provoked a strong reaction from the senior Korean judiciary.⁵⁰

ISA appears to have provoked a reaction in many quarters around the world in recent years, but clearly the most vocal contestation has been in developed democracies such as the European Union, Canada, the United States, Japan, Korea and Australia. These countries, where ISA was seen as affecting only their capital-importing partners of the developing or communist worlds, are now witnessing a number of trade agreements and BITs that can give rise to arbitral claims among themselves. This development has mirrored the increased recourse to ISA in BITs and free trade agreements (FTAs) between developed democracies. As noted above, before the entry into force of NAFTA in 1994, there were very few such agreements between developed democracies. This changed with the adoption of NAFTA — an agreement that binds one developing and two developed countries. It is understood that the United States initiated the move to use its model BIT as the basis for the future Part B of Chapter 11. One may speculate as to what might have ensued had Canada refused to accept this position, but this did not happen, and a robust, fairly detailed form of ISA was built into NAFTA.

⁴⁰ Such organizations include the Council of Canadians (see www.canadians.org/publications for diverse articles criticizing several aspects of NAFTA Chapter 11); Public Citizen (see e.g. *NAFTA Chapter 11 Investor-State Cases: Lessons for the Central America Free Trade Agreement* (Public Citizens Global Trade Watch, 2005); Greenpeace, the Sierra Club of Canada (see www.sierraclub.ca for diverse articles criticizing several aspects of NAFTA Chapter 11) and the World Wildlife Fund (see Julia Ferguson, “California’s MTBE Contaminated Water: An Illustration of the Need for an Environmental Interpretive Note in Article 1110 of NAFTA” (2000) 11 Colorado Journal of International Environmental Law and Policy 499 at 515, quoting David Schorr, director of the World Wildlife Fund’s Sustainable Commerce Program).

⁴¹ On the opposition to NAFTA in Congress, see M Angeles Villarreal & Ian F Ferguson, *The North American Free Trade Agreement (NAFTA)* (Congressional Research Service, 16 April 2015), online: <<https://fas.org/sgp/crs/row/R42965.pdf>>.

⁴² See “Senator Warren Releases Report Highlighting Decades of Broken Promises and Failures to Enforce Labor Standards in Trade Agreements” (18 May 2015), online: <www.warren.senate.gov/?p=press_release&id=819>.

⁴³ See generally Gus Van Harten, *Investment Treaty Arbitration and Public Law* (Oxford: Oxford University Press, 2007).

⁴⁴ See e.g. Gus Van Harten & David Schneiderman, “Public Statement on the International Investment Regime”, 31 August 2010, online: <www.osgoode.yorku.ca/public-statement-international-investment-regime-31-august-2010/>.

⁴⁵ See e.g. Howard Mann, “Reconceptualizing international investment law: Its role in sustainable development” (2013) 17:2 Lewis & Clark Law Review 521.

⁴⁶ See generally Australian Government, Department of Foreign Affairs and Trade, *Gillard Government Trade Policy Statement: Trading Our Way to More Jobs and Prosperity* (April 2011), online: <www.acci.asn.au/getattachment/b9d3cfac-fc0c-4c2a-a3df-3f58228daf6d/Gillard-Government-Trade-Policy-Statement.aspx> and Luke Nottage, “Why No Investor-State Arbitration in the Australia-Japan FTA?” (7 April 2014), *East Asia Forum*, online: <www.eastasiaforum.org/2014/04/09/why-no-investor-state-arbitration-in-the-australia-japan-fta/>.

⁴⁷ As far as the *Australia-United States Free Trade Agreement* of 2005 (AUSFTA) is at stake, the reason for the exclusion of ISA from the agreement put forward by officials of both countries was the “fact that both countries have robust, developed legal systems for resolving disputes between foreign investors and government” (Australian Government, Department of Foreign Affairs and Trade, “Australia-United States Free Trade Agreement: Fact sheets: Investment”, online: <www.dfat.gov.au/fta/ausfta/outcomes/09_investment.html>). Other commentators identified other reasons: “The US was keen to include its modified ISDSM in AUSFTA as well. However, the proposal faced opposition from Australia for two reasons. First, judging by the numerous NAFTA investment cases, if investor-State provisions were to be included in AUSFTA, there would be a strong possibility of numerous suits being initiated against the Australian government by American investors as well. In addition, these NAFTA investment cases had resulted in widespread public resistance to investor-State provisions.” Sachet Singh & Sooraj Sharma, “Investor-State Dispute Settlement Mechanism: The Quest for a Workable Roadmap” (2013) 29:76 (General Issue) Merkourios: International and European Law 88 at 97–98.

⁴⁸ Indeed, while the *Agreement between Australia and Japan for an Economic Partnership* (8 July 2014, online: <investmentpolicyhub.unctad.org/IIA/country/105/treaty/3487>) does not include ISA, the *Free Trade Agreement between Australia and Korea* (8 April 2014, online: <investmentpolicyhub.unctad.org/IIA/country/11/treaty/3433>) does include an ISA clause (arts 11.15ff). It is noteworthy that the recently signed *Free Trade Agreement between Australia and China* (17 June 2015, Section B, online: <investmentpolicyhub.unctad.org/IIA/country/42/treaty/3572>), includes ISA.

⁴⁹ See generally Nottage, *supra* note 46.

⁵⁰ See Phil Taylor, “South Korea: controversy over free trade agreement” (17 January 2012), online: <www.ibanet.org/Article/Detail.aspx?ArticleUid=28f182ef-e2a9-49e9-855c-2d0d19b2d609>.

In the years since NAFTA, the number of BITs or FTAs between developed democracies has grown at a very slow rate, although, at the same time, developed democracies such as Canada and the United States became more accustomed to BITs with ISA as they greatly increased the pace of negotiation of BITs with developing, capital-importing countries.⁵¹

The international Energy Charter Treaty of 1994 was the next major step. The charter links countries of Western and Eastern Europe, the Caucasus and Central Asia. ISA was introduced into this important treaty, which has become the source of a very considerable volume of ISA litigation,⁵² including actions against developed democracies by firms from other democracies.⁵³ There have been a few BITs negotiated in recent years between developed democracies such as the Swiss-Japan Economic Partnership Agreement of 2009.⁵⁴ The most significant increase in numbers came when 12 states of Central Europe emerged as democracies and subsequently joined the European Union. These states had some 190 BITs with major European countries such as Germany, the United Kingdom, France, the Netherlands and Switzerland. Lately, Australia and New Zealand have concluded FTAs including ISA with Korea.⁵⁵ A further extension of the number of agreements with ISA has begun to emerge with the negotiation of major FTAs, including mega-regionals, by the European Union and the United States,⁵⁶ which include both developed democracies and other parties. Thus, over a 20-year period, NAFTA has ceased to be the sole exception and developed democracies have become party to a growing number of ISA commitments *inter se*.⁵⁷

More significant in political terms than the signature of ISA commitments between developed democracies has been the fact that the right to invoke ISA has been exercised by investors. NAFTA has been the second-most invoked ISA procedure after the Energy Charter,⁵⁸ with 19 cases against the United States, and 31 against Canada, compared to 24 against Mexico.⁵⁹ The political reaction against NAFTA Chapter 11 arbitral claims against the United States and Canada has waxed and waned according to the degree of controversy provoked by individual cases, not only in Canada and the United States, but also in other democracies such as Australia, where there has been considerable hostility toward inclusion of ISA in Australian BITs and FTAs. Since the transfer of competence over direct foreign investment to the European Union, there has been a fierce debate,⁶⁰ often fed by reference to the NAFTA experience in the EU Parliament, and recently in Germany and France,⁶¹ to the point that the ISA provisions of CETA appear to be threatened. The governments of Canada and the United States have responded to the criticism of ISA by making changes⁶² to the conduct of NAFTA cases, issuing a note of interpretation⁶³ and subsequently have incorporated these changes and more extensive modifications into other

51 In 2014, Canada signed BITs with Nigeria, Senegal, Mali and Côte d'Ivoire. In addition, in 2015 it signed a BIT with Burkina Faso. Concerning the United States, it signed in 2013 the Trade and Investment Framework Agreement between the United States and CARICOM, the Trade and Investment Framework Agreement between the United States and Libya and, in 2014, the Trade and Investment Framework Agreement between the United States and the Economic Community of West African States.

52 According to UNCTAD, the Energy Charter Treaty is one of the principal sources of global ISA litigation: “The three investment instruments most frequently used as a basis for all ISDS claims have been NAFTA (51 cases), the ECT (42) and the Argentina-United States BIT (17). At least 72 arbitrations have been brought pursuant to intra-EU BITs.” (UNCTAD, *supra* note 21 at 126).

53 An example of such a dispute is the *Vattenfall v Germany* case that involves Vattenfall, a Swedish energy company that has an arbitral claim against Germany, claiming losses resulting from the German government’s decision in 2011 to shut down older nuclear reactors in order to hasten the phaseout of nuclear power generation. For additional information on investment disputes under the Energy Charter Treaty, see generally Thomas Roe & Matthew Happold, *Settlement of Investment Disputes under the Energy Charter Treaty* (Cambridge, UK: Cambridge University Press, 2011).

54 *Japan-Switzerland Economic Partnership Agreement*, 19 February 2009 (entered into force 1 September 2009), online: <www.mofa.go.jp/region/europe/switzerland/epa0902/index.html>.

55 AUSFTA; *New Zealand-Korea Free Trade Agreement*, 23 March 2015, online: <<https://korea.fta.govt.nz>>.

56 One can think in this regard of CETA (*supra* note 5), the TTIP (*supra* note 6) and the TPP (*supra* note 7).

57 Although this number would be greatly reduced if and when the BITs between EU members are abrogated, as they have been advised to do by the commission.

58 See *supra* note 52.

59 See Foreign Affairs, Trade and Development Canada, “NAFTA – Chapter 11 – Investment: Cases Filed Against the Government of Canada”, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/disp-diff/gov.aspx?lang=eng> for the claims filed against Canada; US Department of State, “Cases Filed Against the United States of America”, online: <www.state.gov/s/l/c3741.htm> for the claims filed against the United States; and US Department of State, “Cases Filed Against the United Mexican States”, online: <www.state.gov/s/l/c3742.htm> for claims filed against Mexico.

60 See *supra* note 14.

61 See *supra* note 26.

62 See the second paper in this CIGI ISA series, entitled, “The Impact of the NAFTA Experience on Canadian Policy Concerning Investor-State Arbitration.”

63 See NAFTA Free Trade Commission, *North American Free Trade Agreement: Notes of Interpretation of Certain Chapter 11 Provisions*, 31 July 2001, online: <www.international.gc.ca>.

agreements, especially CETA.⁶⁴ The European Union has followed suit in CETA and other agreements under negotiation. The question outstanding is whether these procedural and substantive changes will satisfy critics of ISA.

A final point should be made. Criticisms of ISA in BITs or investment chapters in RTAs have largely focused on ISA provisions. Very few critics of ISA suggest that the whole investment protection regime should be scrapped. Some critics focus on some of the standards, such as fair and equitable treatment or the restrictions on performance requirements, but generally they appear to be most concerned with the ISA provisions in these agreements.

CRITICISMS LEVELLED AGAINST ISA AND THE ANSWERS THAT MAY BE GIVEN

“ISA is a privilege of foreigners”

A frequent criticism of ISA is that it is an unwarranted privilege given to foreign investors but not enjoyed by domestic investors. The original purpose in creating ISA between developed and developing countries was to put foreign investors and governments on the same footing and make them subject to the same procedural and substantive legal rules in the event of a dispute. Although formally identical and reciprocal, there was originally no expectation that ISA claims would be made against the developed party.

In answer to this criticism, it must be noted that it is not the treaty but domestic law that regulates the treatment of foreign investors. The national law is thus the essential comparator under the treaty and not the treaty itself. Secondly, it is often forgotten that litigation is a very culturally specific experience. Arbitration is uniquely suited to achieving the purpose of avoiding the cultural shock for foreigners of being drawn into the unfamiliar world of a foreign court system. The fears, often quite legitimate, that a court in a developing country may not offer the same guarantees of neutrality, fairness and impartiality that may be expected in a developed democracy, are allayed by recourse to arbitration before judges chosen by the parties who apply procedures and substantive rules known in advance to both sides. Thus, there are strong arguments in favour of ISA between developed and developing countries that explain why the system has emerged as it is. Not all these arguments are accepted by all commentators and governments around the world.

The question addressed in this paper is narrower: do the same arguments prevail between developed democracies? It would be premature to offer a definitive answer to the question at this point. However, the culturally specific nature of litigation in different countries remains a fact between even the most closely allied countries. Litigation in the United States is a daunting prospect for Europeans or Asians — even for Canadians — and there can be little doubt that American investors do not relish the prospect of litigating in foreign languages and in civil law systems where concepts of procedure and evidence vary greatly. ISA provides a neutral forum both as to procedure and substantive law, and guarantees equality of arms. It will certainly not be the only forum available and normally investment-related litigation will take place in specialized administrative, trade and tax courts. But the availability of ISA seems to be welcome in certain situations, especially when no obvious domestic remedy exists, as has happened in a number of NAFTA cases.⁶⁵ One may ask why EU member states have been reluctant to abandon their BITs with new member states formerly part of the Communist Bloc if they are confident that their nationals will receive equal protection under EU law or under the laws of the new member states. But this remains the central question of this study.

⁶⁴ See generally Armand de Mestral, “Exceptions Clauses in the Comprehensive Economic Trade Agreement (CETA) between the EU and Canada: A Model for Future ‘Mega-regional’ Agreements?” (prepared for the Conference on Mega-Regional Trade Agreements, University of Dresden, 23-24 October 2014; forthcoming 2015).

⁶⁵ This was the case in *Abitibibowater Inc v Canada [Abitibibowater]* (legal documents available at Foreign Affairs, Trade and Development Canada, “NAFTA – Chapter 11 – Investment: Cases Filed Against the Government of Canada: AbitibiBowater Inc. v. Government of Canada”, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/disp-diff/AbitibiBowater.aspx?lang=eng>), for instance.

“ISA is designed to favour multinational enterprises over other companies”

It is often alleged that ISA is designed to favour major multinational enterprises (MNEs) and that these corporations have encouraged the emergence of this body of law that especially protects them.

Neither the record of ICSID cases nor the record of arbitral claims under NAFTA fully uphold this claim. The Organisation for Economic Co-operation and Development (OECD) reports that at least 22 percent of ISA claims have involved individuals or small enterprises.⁶⁶ The record of cases under NAFTA involves an even higher number of claims by small and medium-sized enterprises.⁶⁷ Having said this, there can be little doubt that MNEs have encouraged governments to adopt investment protection agreements that contain ISA, in particular those facing arbitrary governmental action or possible expropriation. In doing this, they have found willing supporters in governments around the world, and in major international institutions such as the World Bank and UNCTAD. ISA enjoys the support of MNEs, but the support of states has been essential in building the system.⁶⁸ An important reason why states have negotiated BITs is that the BIT allows an investment dispute to be dealt with directly by the investor and the state concerned rather than requiring the state of the investor to take the political step of espousing the claim of its citizen.

“ISA sets aside recourse to the normal domestic courts, which are competent to deal with investment disputes”

This is another frequent criticism of ISA in a number of developed democracies where it is argued that there is no need for any litigant to bypass the normal domestic court system.⁶⁹ ISA is seen as an unwarranted exemption from the normal democratic principle that all disputes are subject to the duly constituted courts of the land. It is also argued that domestic courts would be fully capable of deciding such disputes and thus should be allowed to do so. Related to this critique is the suggestion that all substantive rights of foreign investors should be framed by domestic law. The government of South Africa appears to have embarked on this process since 2010⁷⁰ and has proposed legislation, currently under public consultation, which would govern the rights and duties of foreign investors, even in the circumstances of arbitration.⁷¹

ISA is an option rather than a requirement, but it certainly does allow the foreign investor to opt out of recourse to the domestic courts. Should this be regarded as an undemocratic privilege or simply the choice of a specialized forum, like so many others that exist? Arbitration is generally recognized today as a valuable and legitimate alternative to courts. Chapter 18 of NAFTA creates a special right of recourse to a binational panel in antidumping and countervailing duties cases, which supplants the Federal Court of Appeal of Canada or the competent courts in the United States and Mexico. It has never been criticized on this ground. Boundary waters issues can be referred by governments to the International Joint Commission under the *Boundary Waters Treaty* of 1909.⁷² This possibility is seldom criticized. Canada accepts the right of recourse to the UN Human Rights Committee for complaints even against domestic court decisions. Canadian citizens are subject to the compulsory jurisdiction of the International Criminal Court for acts committed in Canada and around the world. More generally, it has become common for states to create courts with compulsory jurisdiction over their citizens in

⁶⁶ D Gaukroger & K Gordon, “Investor-State Dispute Settlement: A Scoping Paper for the Investment Policy Community” (2012/13) OECD Working Papers on International Investment at 17, online: <www.oecd.org/daf/inv/investment-policy/WP-2012_3.pdf> (“[f]ar from supporting the view that investment arbitration is not an option for smaller investors, the survey shows that 22% of the claimants in both ICSID and UNCITRAL cases are either individuals or very small corporations with limited foreign operations (one or two foreign projects)”).

⁶⁷ A majority of claims brought under NAFTA Chapter 11 have been initiated by individuals or small companies. See NAFTAclaims.com, online: <www.naftaclaims.com>. On the other hand, it has been reported that the percentage of Fortune 500 companies that brought ICSID cases is about 20 percent (see Leon Trakman & Nicola Ranieri, eds, *Regionalism in International Investment Law* (Oxford: Oxford University Press, 2013) at 268. See also Gaukroger & Gordon, *supra* note 66 at 17–18 (“[e]xtremely large multinationals — those appearing in UNCTAD’s list of top 100 multinational enterprises account for 8% of the total claimants in the ICSID and UNCITRAL samples”).

⁶⁸ See “The Arbitration Game: Governments are souring on treaties to protect foreign investors”, *The Economist* (11 October 2014), online: <www.economist.com/news/finance-and-economics/21623756-governments-are-souring-treaties-protect-foreign-investors-arbitration>.

⁶⁹ See *supra* notes 37–39.

⁷⁰ See *supra* note 18.

⁷¹ In response to criticisms of the insufficient protection proposed in the original bill, the government has now proposed amendments to the Expropriation Act that would weigh the rights and duties of foreign investors under expropriation.

⁷² *Treaty Between the United States and Great Britain Relating to Boundary Waters, and Questions Arising Between the United States and Canada*, 11 January 1909, 36 US Stat 2448, (entered into force 5 May 1910), online: <www.ijc.org/en/_BWT>.

human rights, trade and armed conflict situations.⁷³ Is the fact that all persons in 47 European countries have a direct right of recourse before the European Court of Human Rights (ECHR) (which is currently the most cited court in the world) a violation of democratic principle? Critics of the ECHR in the United Kingdom believe so. But this view is not widely shared in Europe. The CJEU also has broad jurisdiction over economic and related rights of EU citizens and can be approached directly by them.⁷⁴ The Ontario Superior Court and Court of Appeal have both held that the existence of Chapter 11 of NAFTA did not violate the Constitution of Canada, although they said nothing about democratic principle.⁷⁵

Thus, recourse to specialized international tribunals is an increasingly common phenomenon. Just as specialized tribunals are increasingly common within democratic societies and are viewed as essential to the efficient functioning of specialized legal regimes, the mere fact of referring cases to arbitration or creating special international arbitral procedure does not seem to be unacceptable in principle.

Is internalization of the substantive law governing the treatment of foreign investors the answer to the problems seen to exist in ISA? Certainly the more that domestic legislation and administrative process deal with foreign investment in a fair, equitable and evenhanded manner, the less likely it is that disputes will arise. In theory, at least, there is much to commend this approach. However, it does presuppose general commitment to roughly the same substantive and procedural standards. This would imply that all governments of the world would proceed to adopt a domestic law governing foreign investment that would contain standards comparable to those found in existing international law. One may doubt that such a degree of uniformity is attainable in the world as it is today.

“ISA offends normal domestic constitutional principles”

It is alleged by some⁷⁶ that the mere fact of recourse to ISA is a violation of normal domestic constitutional principles. This position may be based on the view that any recourse outside domestic courts is improper, or that the choice of ISA itself is the problem in that it is seen as inviting challenges to domestic law.

Recourse to international tribunals by governments and private parties is becoming more common. This does not definitively answer the question posed as to democratic principle. Each case must be argued on its merits, but the mere fact of recourse to arbitration is surely not of itself a violation of democratic principles. Can the same be said of the creation of a special international legal remedy? One way to approach this issue would be to follow the logic of the German Constitutional Court, which has been asked whether certain changes to the European Union treaties violate democratic principles. The court has answered this in a series of judgments essentially suggesting that, without constitutional amendment, Germany could not abdicate vital governmental functions to the European Union, and the court has set out a number of red lines that cannot be crossed without constitutional amendment.⁷⁷ EU competences now include the regulation of foreign direct investment and adjudication on such issues by the CJEU.⁷⁸ The German Constitutional Court has never suggested that this transfer of authority violates fundamental democratic principles. More generally, it would seem surprising in the twenty-first century to suggest that the option of recourse to a specialized international judicial forum should be denied to democratic governments. The question must surely turn on the nature of the ISA process itself. The criticisms of the ISA process and rules are discussed below.

73 See generally Karen Alter, *New Terrain of International Law: Courts, Politics, Rights* (Princeton: Princeton University Press, 2014).

74 TFEU, *supra* note 27, art 263.

75 See *Council of Canadians v Canada (AG)*, [2005] OJ no 3422 (Sup Ct), online: <www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/disp-diff/cupw-13.pdf> and *Council of Canadians v Canada (AG)* (2006), 217 OAC 316, 277 DLR (4th) 527, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/disp-diff/cupw-17.pdf>.

76 See e.g. *An Open Letter From Lawyers to the Negotiators of the Trans-Pacific Partnership Urging the Rejection of Investor-State Dispute Settlement*, 8 May 2012, online: <<https://tpplegal.wordpress.com/open-letter/>>.

77 On these questions, see generally Erich Vraneš, “German Constitutional Foundations of, and Limitations to, EU Integration: A Systematic Analysis” (2013) 14:1 German Law Journal 75.

78 Beside the explicit inclusion of the EU’s exclusive competence to sign international agreements affecting FDI in the TFEU (see *supra* note 27), it is noteworthy that the EU institutions had already entered into IIAs via the doctrine of implied powers whereby the European Union is competent to act internationally in fields where such a competence, while not being provided by the treaties, is essential to exercise internal competences efficiently and pursue the objectives of the treaties. This doctrine is incorporated in article 3(2) of the TFEU (see also article 64(2) of the TFEU), but was developed as soon as 1970 in the *AETR* case (*Commission v Council*, C-22/70, [1971] ECR 263) in which the ECJ stated that the authority to enter into international agreements “arises not only from an express conferment by the Treaty but may equally flow implicitly from other provisions of the Treaty, from the act of accession and from measures adopted within the framework of those provisions, by the Community institutions.”

Until the mid-part of the twentieth century, judges in a number of countries, including Canada, showed considerable hesitation in allowing and enforcing judgments by arbitrators. But as a result of legislative intervention and a change of approach, judges in Canada and most democratic countries accept and enforce arbitral decisions without question as to their legitimacy. Arbitration and other forms of alternative dispute resolution have become a valuable, and in some cases obligatory, alternative to recourse to the crowded court dockets.

One can argue that ISA is a special case in that it involves a unique mix of private and public interests. This is a central issue. As recently as 2005, judges of the superior courts of Korea expressed serious reservations as to the legitimacy of ISA.⁷⁹ But after a period of study they appear to have withdrawn their reservations. Senior members of the legal community in Australia and New Zealand, among others, expressed similar concerns in a petition in 2012.⁸⁰ The current Australian government does not appear to share all these reservations and has recently concluded a trade agreement that includes ISA provisions.⁸¹

Arguably, the mere fact of mixing public and private interests in an arbitration does not necessarily make the process illegitimate. Recent decisions by the Supreme Court of the United States have held that competition law issues may legally be subjected to arbitration between private parties.⁸² The CJEU appears to hold a similar view,⁸³ as does the Supreme Court of Canada.⁸⁴ There does appear to be a developing policy allowing the arbitration of an increasing range of public issues in litigation between private parties. This certainly remains a sensitive issue and some critics of ISA suggest that it crosses the line. But if one considers these arguments in light of the ever-expanding role of arbitration in a great many forms of litigation, these arguments of principle against arbitration are now unlikely to prevail.

“ISA is conducted in secret and ISA procedures are generally non-transparent”

Arbitration involves the choice of privately selected judges who are authorized to render a legally binding decision. Once invoked, the choice of arbitration is irrevocable. Commercial arbitration almost always takes place in a private and confidential environment. This is thought to be one of the advantages of arbitration, together with efficacy, speed, lower costs and the right to choose the procedure and applicable law. When ISA was first established, it was assumed that the proceedings would be private and confidential and that the award need not be made public, absent agreement among the parties. Some arbitral administering organizations such as the London Court of International Arbitration (LCIA),⁸⁵ which as of today does not administer ISAs, and the International Chamber of Commerce (ICC),⁸⁶ which has administered a relatively small number of investor-state proceedings, continue to conduct arbitrations on this basis. The widely used United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules⁸⁷ do not necessarily require public proceedings or publication of awards, although great progress has been made in this regard with the adoption of the UNCITRAL Rules on Transparency, to which parties can agree.⁸⁸ Regarding the ICSID Arbitration Rules, it is noteworthy that they have been amended

79 See “Strange judges”, *Korea Herald* (12 December 2011), online: <www.koreaherald.com/view.php?ud=20111212000383>.

80 *Supra* note 76.

81 See *supra* note 48.

82 See e.g. *Mitsubishi Motors Corp v Soler Chrysler-Plymouth, Inc*, 473 US 614 (1995).

83 See International Bar Association, *IBA Private Enforcement: Arbitration*, at 6: “There has been a discussion in the legal doctrine over the years as to whether EC competition law may be subject to hearings in arbitration. The general opinion should now be that this is the case and that, accordingly, competition law is arbitrable. This would also be confirmed by the ECJ in i.a. the cases *Nordsee* [Case 102/81] and *Eco Swiss/Benetton* [Case C-126/97].”

84 See e.g. *Desputeaux v Editions Chouette (1987) inc*, 2003 SCC 17, [2003] 1 SCR 178; *Dell Computer Corp v Union des consommateurs*, 2007 SCC 34, [2007] 2 SCR 801; *Rogers Wireless v Muroff*, 2007 SCC 35, [2007] 2 SCR 921; and *Bisaillon v Concordia University*, 2006 SCC 19, [2006] 1 SCR 666.

85 *LCIA Arbitration Rules (2014)*, online: <www.lcia.org/Dispute_Resolution_Services/lcia-arbitration-rules-2014.aspx#Article%2014>.

86 *ICC Rules of Arbitration*, 2012, online: <www.iccwbo.org/Products-and-Services/Arbitration-and-ADR/Arbitration/Rules-of-arbitration/Download-ICC-Rules-of-Arbitration/ICC-Rules-of-Arbitration-in-several-languages/>.

87 *UNCITRAL Arbitration Rules (as revised in 2010)*, online: <www.uncitral.org/uncitral/en/uncitral_texts/arbitration/2010Arbitration_rules.html>.

88 It is noteworthy that on 17 March 2015, the Mauritius Convention (*United Nations Convention on Transparency in Treaty-based Investor-State Arbitration*, adopted 10 December 2014) was open for signature. The Mauritius Convention is an instrument by which the parties to investment treaties concluded before 1 April 2014 express their consent to apply the UNCITRAL Rules on Transparency.

to require greater transparency.⁸⁹ Thus, many investor-state proceedings continue to be conducted in private, at the behest of the parties.

Many forms of commercial arbitration are indeed conducted in secret and the decisions remain confidential, although they normally have to be made public if a party goes to court to seek enforcement. It is of the nature of commercial arbitration that parties should have the flexibility to choose the procedures and where and how they will be conducted, including privacy. The question is whether all these assumptions can and should be transferred to ISA. Many parties — governmental and private — prefer that ISA proceedings be confidential and conducted in private. This has been particularly the case with respect to developing countries. The rules of procedure of many administering authorities, such as the LCIA, provide for the rule of confidentiality and many arbitrations under the UNCITRAL Rules remain confidential even if progress has been made in the field of ISA.⁹⁰

There has been widespread criticism of confidential proceedings and confidential arbitral awards in developed democracies, first with respect to NAFTA⁹¹ and subsequently in the European Parliament, where it has been argued that proceedings involving public and private interests should always be heard in public, as is the case in proceedings before domestic courts. Thus, there is serious challenge to the simple transposition of the understandings surrounding commercial arbitration to the universe of ISA.

In response to criticisms of the secrecy of proceedings, much in fact has happened. In direct response to criticisms, the parties to NAFTA decided to make all pleadings, hearings and decisions public within a few years of NAFTA entering into force.⁹² ICSID, the principal body administering ISA procedures, has taken significant steps in the same direction.⁹³ The facts of a claim are public and, in principle, pleadings and hearings and awards are all public, although it is still possible for a party to refuse permission to the publication of an award. In a further important step, UNCITRAL adopted its rules on transparency in 2014.⁹⁴ If generally adopted in UNCITRAL proceedings and incorporated into others, this convention will go far in making ISA procedures public. Finally, and perhaps most significant, model BITs of Canada,⁹⁵ the United States⁹⁶ and Norway,⁹⁷ among others, have incorporated principles of transparency. These principles have been written into the BITs of a number of these countries' recent BITs,⁹⁸ and the trend toward mega-regionals involving the European Union and the United States⁹⁹ clearly follows this approach. Thus, while there are non-transparent procedures that still exist, it would appear that the principal democracies will not sign a BIT that does not incorporate broad principles of transparency.

“ISA is conducted by arbitrators with bias and who serve several masters and have no understanding of domestic values”

Concern is often expressed that the pattern of nomination and activity that characterizes commercial arbitration is followed in the practice of ISA. Arbitrators are named for their known skill in managing arbitrations. Many concerns focus on the persons who become arbitrators; it is alleged that they are

89 The ICSID Arbitration Rules were modified and became effective on 10 April 2006. The new rules include improvements concerning the transparency of proceedings among which are: the possibility for tribunals to consider requests from third parties to file amicus briefs (Arbitration Rule 37); the opening of an ICSID hearing to the public (Arbitration Rule 32); and the requirement for ICSID to “promptly” publish “excerpts of the legal reasoning” of every award (Arbitration Rule 48).

90 See *supra* note 87 and accompanying text and two following paragraphs.

91 See Nicola W Ranieri, “Investors’ Rights, Legal Concepts, and Public Policy in the NAFTA Context” in Trakman & Ranieri, *supra* note 67 at 411.

92 See the FTC’s Notes of Interpretation, *supra* note 63.

93 In this regard, it is noteworthy that the ICSID amended its Arbitration Rules in 2006. See generally Jason W Yackee & Jarrod Wong, “The 2006 Procedural and Transparency-Related Amendments to the ICSID Arbitration Rules: Model Intentions, Moderate Proposals, and Modest Returns” in Karl P Sauvant, ed, *The Yearbook on International Investment Law and Policy* (Oxford: Oxford University Press, 2010) ch 6.

94 The UNCITRAL Rules on Transparency came into effect on 1 April 2014 and comprise a set of procedural rules that provide for transparency and accessibility to the public of treaty-based investor-state arbitration. See also *supra* note 88 on the Mauritius Convention, which is now open for signature and which has for effect to bind the parties to the convention to apply the UNCITRAL Rules on Transparency.

95 Canadian Model FIPA, art 38.

96 US Model BIT, art 29.

97 Norway Model BIT, art 19.

98 See e.g., for Canada, the Canada-Côte d’Ivoire BIT (2014), art 30; the Canada-Mali BIT (2014), art 30; and the Canada-Senegal BIT (2014), art 31. For the United States, see e.g. art 29 of the US-Rwanda BIT (2008).

99 See e.g. CETA, art X.33(1) (“Transparency of Proceedings”) of Chapter 10. See also art X.34 (“Sharing of Information”) of the same chapter and art II.23 of the TPP’s leaked investment chapter.

chosen from a very small and unrepresentative group who have expertise in law, but no expertise in the broader social, economic or environmental issues of public policy that are often posed in ISA. Particularly disquieting to many is the fact that some, but by no means all, arbitrators also serve as counsel in other cases and may thus be perceived to have a personal interest in accepting or promoting certain arguments over others. In short, there is a perception of systemic or personal bias. More broadly, there is a concern that arbitrators are unprepared or even personally unwilling to deal with the broad policy issues that may be posed in ISA cases and there is a strong feeling that the paradigm of international commercial arbitration is unsuitable for ISA cases that pose public policy questions as well as private commercial interests, and there is a fear that the private commercial interests will always prevail.¹⁰⁰ There is also the concern that very few arbitrators are women.

A first answer to these objections concerning arbitrators is that each party has the complete right to choose the arbitrator they wish. Nothing prevents states from choosing experts in social or environmental policy as their nominee, and from insisting on the nomination of a suitably qualified chair of the panel. Unless no such persons exist, which is hard to believe, states can in fact select arbitrators who they believe will be sympathetic to the positions they adopt. This is of the very essence of arbitration. If parties cease to have the right to select their arbitrators, the process will be radically different. Until now, the assumption has been that the best arbitrators are those who have distinguished themselves in conducting commercial or public international arbitration either as arbitrators or advocates. If there is a concern that commercial arbitrators are likely to be biased in favour of the private foreign investor, other persons can certainly be found. A less radical approach would be to select as arbitrators only those who have never served as counsel and who act only as arbitrators. The drawback of this approach is that it would restrict the pool of arbitrators to elder statesmen and women who are sufficiently advanced in their careers, or academics, so that their income is less of an issue. It may not be easy for most professional arbitrators to serve in a single capacity and yet remain able to cover the costs of expensive offices and remain fully aware of developments in the law, unless they are guaranteed a steady stream of nominations. This, in turn, would only accentuate the phenomenon of concentration of arbitrations in the hands of a small group of persons — itself a source of considerable complaint.

A further fact that critics do not always consider is that arbitrators are expected to be faithful to the law they apply. Certainly the arbitrators with the highest reputation are those who have a deep understanding of the law that they apply and a commitment to apply that law only. This ideal may not be achieved in all cases but is the essence of their professional commitment. This may not satisfy critics, but there is little evidence that most arbitrators do not have a profound commitment to the law they apply.

A further answer to critics under this head is to suggest that they may be aiming at the wrong target and their real complaint should be against the law being applied rather than the arbitrators who apply it. In answer to this concern, governments have been responding by steady amendments to the law. The United States, Canada, Norway and many others have adopted model BITs that contain extensive amendments to the traditional European gold standard agreements. Provisions in these models make a variety of important changes:

- the procedures ensure a much greater degree of transparency;
- substantive standards of protection of investments such as fair and equitable treatment and full protection and security are refined to limit their scope;
- the definition of direct and indirect expropriation is refined and limited;
- states are given the power to weed out unmeritorious cases;
- states are given power to make binding interpretations of the scope of various provisions;

¹⁰⁰ See Susan D Franck et al, “The Diversity Challenge: Exploring the ‘Invisible College’ of International Arbitration” (2015) 53 Columbia Journal of Transnational Law 429, online: <papers.ssrn.com/sol3/papers.cfm?abstract_id=2611214>; Chiara Giorgetti, “Who Decides Who Decides In International Investment Arbitration?”, (2013) 35 University of Pennsylvania Journal of International Law 431, online: <scholarship.richmond.edu/cgi/viewcontent.cgi?article=1893&context=law-faculty-publications>.

- the national treatment and MFN standards are limited so as to protect the right of states to protect public health, the environment, etc.; and
- clearer and broader exceptions clauses are written in to protect the right of states to adopt regulatory standards of various kinds.

One of the best examples, and probably a model of things to come in the future, is to be found in the CETA text announced by Canada and the European Union in 2014. The very extensive revisions of the traditional model go a long way toward answering critics and are clearly designed to ensure that democratic governments continue to make public policy and express this policy in binding laws, regulations and decisions.

One issue on which the critics make a very fair point concerns the number of women acting as arbitrators. With some very notable exceptions, women have been under-represented among arbitrators.

“What we need is a global arbitration appeal court like the Appellate Body of the World Trade Organization, or a fixed roster of arbitrators”

ISA awards are often criticized as being unpredictable, since each arbitration is a separate case on its own facts and since there is no theory of *stare decisis* in ISA proceedings. Critics point to a number of cases, some arising on the same facts,¹⁰¹ others dealing with similar legal issues such as the justification of necessity.¹⁰² This criticism is related to the criticism that is made against the very process of arbitration and by the alleged vagueness of ISA standards. It is often argued that the absence of any kind of appeal mechanism, comparable to the Appellate Body (AB) of the World Trade Organization (WTO), is a fatal flaw to the legitimacy and coherence of ISA law. There is no international tribunal that is empowered to review ISA awards for errors of fact or law, and it is alleged that those more limited procedures that do exist, particularly the ICSID ad hoc annulment committee procedure¹⁰³ or the ICC Court of Arbitration¹⁰⁴ are ineffective or too limited in scope to respond to the fatal flaws that exist in the ISA system. Critics taking this position call for the creation of a universal ISA appeals court or at least the constitution of a very limited roster of arbitrators whose judgment could be trusted.

It is argued that the existence of an arbitral court of appeal for all ISA decisions would bring a new degree of uniformity and predictability to decisions, since arbitrators would be required to follow the court of appeal or have their decisions challenged and corrected on appeal if they failed to do so. It is also argued that a court of appeal focusing entirely on ISA matters would be more likely to steer ISA law in the right direction and get difficult cases right. The WTO AB is seen as a model to be adopted. Alternatively it is suggested that if all arbitrators were chosen from a roster pre-selected by states there would be much more confidence in the decisions rendered by these people.

At first blush, these suggestions have much to commend them and are supported by some governments. They have, in fact, been proposed in various texts. The US model BITs, as well as such texts as CETA, contain a reference to the possibility of creating an appellate court in the future.¹⁰⁵ Along the same lines, efforts were made some 10 years ago to amend the ICSID Convention ad hoc annulment committee procedure, which currently allows for the annulment of ICSID awards on a limited number of grounds by a panel of three ICSID arbitrators chosen by the chairman of the administrative council from the

101 Such a situation can be exemplified by the *Lauder* (*Lauder v The Czech Republic* (2001), 9 ICSID Reports 66, (2002) 14 World Trade and Arbitration Materials 35 [*Lauder*]) and *CME* (*CME Czech Republic BV v Czech Republic* (2003), 15(4) World Trade and Arbitration Materials 83) arbitrations that dealt with similar factual circumstances.

102 See e.g. *CMS Gas Transmission Company v Argentina* (2003), 42 ILM 788 (ICSID) at para 86:

The Tribunal notes in respect that the Centre has made every effort possible to avoid a multiplicity of tribunals and jurisdictions, but that it is not possible to foreclose rights that different investors might have under different arrangements. The Tribunal also notes that, while it might be desirable to recognize similar rights to domestic and foreign investors, this is seldom possible in the present state of international law in this field. Finally, it is not for the Tribunal to rule on the perspectives of the negotiation process or on what TGN might do in respect of its shareholders, as these are matters between Argentina and TGN or between TGN and its shareholders.

103 See art 52 of the ICSID Convention (*Convention on the Settlement of Investment Disputes Between States and Nationals of Other States*, 18 March 1965, 17 UST 1270, TIAS 6090, 575 UNTS 159).

104 See “Appendix I – Statutes of the International Court of Arbitration”, ICC Arbitration Rules, online: <www.iccwbo.org/Products-and-Services/Arbitration-and-ADR/Arbitration/Rules-of-arbitration/ICC-Rules-of-Arbitration/>.

105 CETA, *supra* note 5, art X.42(1)(c) (Chapter 10).

panel of arbitrators appointed by ICSID member states. It was proposed¹⁰⁶ to change this rather limited and blunt procedure into a genuine appeals process for the entire ICSID Convention. This would have covered a large number of ISA awards and had the potential to bring about a major change in ICSID law. As of 2015, ICSID has administered 70 percent of all ISA arbitrations. The annulment committee process only applies to arbitrations conducted under the ICSID Convention Rules and not under the Additional Facility Rules, so it does not reach all arbitrations administered by ICSID. Unfortunately, there was no support among the broad membership of ICSID; the proposal is currently dormant,¹⁰⁷ but efforts are now under way to revive it. The greatest difficulty will be for any amendment of the ICSID Convention to receive unanimous support in order for it to be implemented.

The creation of an appeals tribunal for all 3,200 BITs and FTAs is an utterly daunting task and would be impossible to achieve. The only way to achieve this would be to revive the Multilateral Agreement on Investment (MAI), which died for want of support in 1998.¹⁰⁸ Another possibility, albeit much more limited, would be the creation of individual appeals processes for major new initiatives such as CETA, the TTIP or the TPP. A further possibility would be the submission of all ISA complaints to a single international court. The likelihood of being adopted is slight.

The establishment of a fixed roster of trusted arbitrators to be chosen to hear all ISA cases is sometimes proposed as a means of enhancing public trust in the ISA process. There are a number of obvious objections, including perceptions of bias against private investors, which make this approach unpalatable.

A further refinement would be a standing roster of arbitrators to serve as judges in a general appeals procedure. This is also an interesting approach but suffers from the difficulties of giving jurisdiction to a single appeals court discussed above.

In conclusion, while a universal court of appeal is an idea that has much to commend it, the practical and political difficulties in the way of its creation may prove to be insuperable.

“ISA allows foreign companies to challenge normal domestic regulation”

This is perhaps the central and most pervasive criticism that has emerged since the entry into force of NAFTA Chapter 11. Some critics consider that ISA claims constitute a challenge to the right of states to regulate and to make public policy choices. This sentiment has recently been voiced by German officials¹⁰⁹ with respect to the claim by the Swedish Vattenfall Corporation alleging economic loss in Germany as a result of the decision of the German federal government to shut down nuclear reactors. Similar sentiments appear on the website of the governing French Socialist Party¹¹⁰ with respect to the ISA provisions in CETA. ISA provisions in treaties are thus seen as an unwarranted and unwelcome invitation to foreign private interests to challenge public policy. Critics also point to the fact that over the years ISA cases have involved claims that relate to the exercise of regulatory measures dealing with a very wide range of sensitive public policy measures, and that claims frequently involve huge sums of money.

One partial answer to this criticism is that ISA does not allow a challenge of a public policy *as such*; this happens under the WTO Dispute Settlement Understanding in which a state is asked to withdraw the measure.¹¹¹ BITs allow the foreign investor to claim damages only for breach of a treaty standard. There is no obligation on a state to withdraw a measure, as is the case in the WTO. Secondly, it should be noted that an ISA challenge is not to the legality of a measure *as such*, but only claims that the measure

106 ICSID Secretariat, “Possible Improvements of the Framework for ICSID Arbitration” (2004) ICSID Discussion Paper, online: <<https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/Possible%20Improvements%20of%20the%20Framework%20of%20ICSID%20Arbitration.pdf>>.

107 See ICSID Secretariat, “Suggested Changes to the ICSID Rules and Regulations” (2005) ICSID Working Paper, online: <<https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/Suggested%20Changes%20to%20the%20ICSID%20Rules%20and%20Regulations.pdf>> and Katia Yannaca-Small, “Improving the System of Investor-State Dispute Settlement” (2006/01) OECD Working Papers on International Investment.

108 See Dolzer & Schreuer, *supra* note 10 at 26–27.

109 See Sebastian Knauer, “Vattenfall vs. Germany: Power Plant Battle Goes to International Arbitration” (15 July 2009), *Spiegel Online International*, online: <www.spiegel.de/international/germany/vattenfall-vs-germany-power-plant-battle-goes-to-international-arbitration-a-636334.html>.

110 See “TAFTA (TTIP) et CETA: la position des socialistes” (4 February 2015), online: <www parti-socialiste.fr/articles/tafta-ttip-et-ceta-la-position-des-socialistes>.

111 WTO, *Understanding on Rules and Procedures Governing the Settlement of Disputes*, Annex 2, art 3.7.

fails to meet the standard set by the treaty. A further point that can be made that, at least in democracies subject to the rule of law, claims are made before domestic courts against all kinds of public policy every day of the week. The same German minister of industry who objects to Vattenfall's arbitral claim as an attaint to German sovereign right to make energy policy, does not appear to see any impropriety in the fact that German nuclear energy companies are complaining about the same measure before the German courts.

The objection, therefore, must be against ISA as a process and not against the right to challenge public policy. Here it must be admitted that a court seems to enjoy a greater degree of legitimacy in the public eye. A good example is the case law of the CJEU concerning the action in damages for serious violations of EU law by member states.¹¹² In creating the action in damages against member states for serious breaches of EU law, the CJEU took care to balance the rights of those suffering economic loss against the interests of states as economic regulators, something that arbitrators have trouble articulating openly, due to their limited mandate. But, in conclusion, the mere fact of an action in damages based on the abuse of regulatory powers is hardly a novelty in democratic societies.

"ISA process unduly restrains domestic regulatory options and threatens environmental, labour and human rights standards: it leads to a 'regulatory chill'"

The previous criticism frequently takes the form of the allegation that the existence of potential ISA claims acts as a "regulatory chill." This criticism was first advanced in Canada by Howard Mann writing for the IISD¹¹³ and has subsequently been taken up by Gus van Harten in his books¹¹⁴ as well as Elizabeth May, leader of the Green Party of Canada,¹¹⁵ and labour unions.¹¹⁶ Similar criticism, in virtually the same terms, has been voiced in the debates of the European Parliament and by other European public interest groups since the transfer of competence over foreign direct investment to the European Union.¹¹⁷ In Japan, ISA in the TPP is seen as a threat to the integrity of Japanese agriculture. Similar sentiments have been strongly voiced by the legal community in Australia.¹¹⁸

Central to these concerns is the fear that public policies in favour of environmental protection, public health, employment in the public sector, agricultural production policies and human rights standards may be particularly subject to challenge. As a result of this potential challenge, it is alleged that governments and public servants will be reluctant to adopt new regulations in the public interest. Critics point to various challenges to environmental regulations under NAFTA

112 See e.g. *Francovich v Italy and Bonifaci and Others v Italy*, Joined Cases C-6/90 and C-9/90, [1991] ECR I-5357, , online: <eur-lex.europa.eu/resource.html?uri=cellar:7a76ea3f-a919-475c-8cbe-29e0b260ebc4.0002.03/DOC_1&format=PDF>; *The Queen v Secretary of State for Transport, ex parte: Factortame Ltd and Others*, Case C-213/89, [1991] ECR I-3905, online: <eur-lex.europa.eu/resource.html?uri=cellar:ff8d6d63-022c-4f23-9cea-4c79f37ca53f.0002.03/DOC_2&format=PDF>; *Brasserie du Piecheur SA v Germany and The Queen v Secretary of State for Transport*, Joined Cases C-46/93 and C-48/93, [1996] ECR I-1029, online: <eur-lex.europa.eu/resource.html?uri=cellar:c282fcda-29a2-4ba5-99a6-da45b05cb305.0002.03/DOC_1&format=PDF>.

113 Mann, *supra* note 45.

114 Van Harten, *supra* note 43.

115 See Elizabeth May, "What happened under Chapter 11 of NAFTA?" (17 May 2013), online: <elizabethmaymp.ca/investor-state-treaties/what-happened-under-chapter-11-nafta>.

116 See *supra*, footnote 40.

117 See e.g. European Trade Union Confederation, "ETUC Resolution on EU Investment Policy" (2013), online: <www.etuc.org/documents/etuc-resolution-eu-investment-policy> and Trade & Investment, "Public interest, social and environmental policies under threat: Change EU investment policy: now is the time!" (January 2011), online: <www.tni.org/sites/www.tni.org/files/download/Investment_Briefing_S2B-et-al_Jan2011.pdf>. See also *supra* note 17.

118 See generally Australian Government, *supra* note 46. See also Adam Bender, "TPP: Australia pushes against ISDS in trade agreement, WikiLeaks reveals" (26 March 2015), online: <www.computerworld.com.au/article/571302/tpp-australia-pushes-against-isds-trade-agreement-wikileaks-reveals/>.

Chapter 11,¹¹⁹ as well as the challenge to plain packaging legislation in Australia and Uruguay¹²⁰ and various cases against Ecuador taken by oil companies.¹²¹ The argument of a potential regulatory chill from ISA is advanced generally, although some critics suggest that it is particularly serious with respect to small, developing countries that may have difficulty defending themselves.

There is little convincing evidence of a regulatory chill leading to a reluctance to adopt new environmental or labour standards, etc. The allegation is pervasive: proof is very scarce. The fear of action under NAFTA Chapter 11 did not deter Canadian Minister of the Environment Sheila Copps from closing the border to the importation of fuel-additive MMT,¹²² and the export of nuclear wastes.¹²³ Similarly, the quasi certainty of legal action did not deter Newfoundland and Labrador from expropriating the assets of Bowater.¹²⁴ There is no evidence that the European Union or the United States have been cowed by the possibility of ISA. Thus, there is no credible evidence that the developed democracies included in this study have been affected.

What is more credible is that the threat of ISA proceedings may act as a deterrent to small, developing countries. This is often alleged and in support it can be noted that Uruguay sought financial support from Bloomberg Philanthropies and the Bill and Melinda Gates Foundation to fund its defence against Philip Morris International.¹²⁵ It had previously adopted its plain packaging laws despite objections from the tobacco company. But hard evidence is difficult to obtain and the whole debate remains mainly anecdotal.

A further important point is that, under NAFTA Chapter 11, states have lost very few cases. This is particularly true of developed democracies. The United States has never lost a case. Until the Bilcon¹²⁶ decision, Canada had never lost a case that did not appear to involve clear discrimination in trade law terms or uncompensated expropriation. It is true that Mexico has lost a larger percentage of cases.¹²⁷ There have been no cases reported against Japan and a first case has only recently been initiated against Korea.¹²⁸ Australia has been sued only once. The claim by the Philip Morris corporation has received a great deal of publicity and has done much to bring ISA into disrepute in Australia. But it is almost certain that Australia will win this arbitration. The European Union has never been sued, although several member states of Eastern Europe have been sued in situations involving allegations of discriminatory governmental action against foreign investors.¹²⁹ Virtually all of these cases have been lost by the states defending their regulatory measures, suggesting that the allegations by foreign investors of bias and discrimination were well founded, and they give some credit to the Canadian desire to include ISA in the CETA investment chapter (Chapter 10). Far more controversial, from the political and policy

¹¹⁹ See e.g. *Ethyl Corporation v Canada* [Ethyl], online: <www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/disp-diff/ethyl.aspx?lang=eng>; *SD Myers, Inc v Canada*, Partial Award, 13 November 2000 [SD Myers], online: <www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/disp-diff/myers-18.pdf>; *Methanex Corporation v United States*, 3 August 2005 [Methanex], online: <www.italaw.com/sites/default/files/case-documents/ita0529.pdf>; *Metaleclad Corporation v Mexico* (2000), 40 ILM 36 (ICSID) [Metaleclad], online: <www.italaw.com/sites/default/files/case-documents/ita0510.pdf>; *Chemtura Corporation (formerly Crompton Corporation) v Canada*, Award, 2 August 2012, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/disp-diff/chemtura-14.pdf>; *Waste Management, Inc v Mexico* (2004), 40 ILM 36 (ICSID) [Waste Management], online: <www.italaw.com/sites/default/files/case-documents/ita0900.pdf>; *Dow AgroSciences LLC v Canada*, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/disp-diff/agrosciences.aspx?lang=eng>; *Clayton v Canada*, Award on Jurisdiction and Liability, 17 March 2015, PCA Cas No 2009-04 [Clayton], online: <www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/disp-diff/clayton-12.pdf>.

¹²⁰ See *Philip Morris Brands Sàrl, Philip Morris Products SA and Abal Hermanos SA v Uruguay*, ICSID Case No ARB/10/7, online: <www.italaw.com/cases/460> and *Philip Morris Asia Limited v Australia*, PCA Case No 2012-12, online: <www.italaw.com/cases/851>.

¹²¹ See e.g. *Murphy Exploration and Production Company International v Ecuador*, ICSID Case No ARB/08/4, online: <www.italaw.com/cases/723> and *Occidental Petroleum Corporation Occidental Exploration and Production Company v Ecuador*, ICSID Case No ARB/06/11, online: <www.italaw.com/cases/767>.

¹²² See *Ethyl*, *supra* note 119.

¹²³ *Waste Management*, *supra* note 119.

¹²⁴ *Abitibibowat*, *supra* note 65.

¹²⁵ See Kadhim Shubber, “Bloomberg and Gates launch fund to fight Big Tobacco”, *Financial Times* (18 March 2015), online: <www.ft.com/intl/cms/s/0/abc75c04-cd5a-11e4-9144-0014feab7de.html#axzz3aWWwxayb>.

¹²⁶ See *Clayton*, *supra* note 119.

¹²⁷ Among the NAFTA cases that have been decided, Mexico has lost close to 50 percent of its cases. See “Disputes with Mexico”, online: NAFTAclaims.com <[www.naftaclaims.com/disputes-with-mexico.html](http://NAFTAclaims.com/disputes-with-mexico.html)>.

¹²⁸ *LSF-KEB Holdings SCA v Korea*, ICSID Case No ARB/12/37 (no document publicly available). See also “\$4.68B Lone star versus Korea Hearing begins in Washington DC”, *The Korea Times* (15 May 2015), online: <www.koreatimesus.com/first-hearing-opens-over-lone-star-asset-sell-offs-in-korea/>.

¹²⁹ Members of Eastern Europe that have been respondent in investor-state arbitrations include Estonia, Hungary, Romania, Bulgaria, Poland, Slovenia, Lithuania and the Czech Republic. For an exhaustive list of member states of the European Union that have been respondents in ICSID proceedings, see *supra* note 29 at 26–27.

perspective, are the actions currently pending against Spain, all flowing from disputes arising out of the cancellation of solar energy supply contracts. These cases are seen as evidence of the dangers of ISA commitments in the face of economic difficulties and their outcome may weigh heavily in the coming policy debate in the European Union.

The expectation regarding ISA claims against developed democracies originally suggested that these states would not be sued at all or would come out the strong winners. The basic paradigm of ISA was created for the protection of foreign investments in developing countries. This picture has grown more complex in recent years, as more agreements provide for ISA between developed democracies.

“ISA standards of protection are open to all kinds of abusive interpretation”

Another significant criticism of ISA focuses not on the procedure but on the substantive standards of protection set out in various investment treaties such as NAFTA Chapter 11. It is argued that these standards, such as national treatment, most favoured nation treatment, fair and equitable treatment, full protection and security, prohibition of certain “performance requirements” and the prohibition of expropriation without full and prompt compensation, are very difficult to define and are thus subject to overly expansive interpretation. The result of this ambiguity is that it is feared that arbitrators can expand the definitions indefinitely with a view to protecting private interests. In support of this argument, critics point to various decisions under NAFTA Chapter 11 and other treaties interpreting the fair and equitable treatment standard and suggest that it is subject to almost infinite expansion at the discretion of arbitrators. The result of the ambiguity of the substantive rules is that governments can never be sure that their laws and decisions will not be subject to challenge by foreign investors.

Finally, there is the fear that hedge funds or some law firms may seek out potential claims and offer to fund and manage them on a contingency basis, thus increasing the possibility that claims will be made.

A first point that should be made is that arbitrators are bound by their mandate, the law and their professional ethics; they are not permitted to give way to personal prejudices. Furthermore, arbitrators are appointed to the panel to serve the interests of justice, not the interests of the party that nominates them. Any arbitrator who departs from this standard debases the whole process. It may happen, but in the main arbitrators serve with a high degree of professional and ethical conduct. The second point is that observers of ISA should not equate the claim with the final award. Advocates make big claims, but are seldom awarded anything close to their claim when they succeed.¹³⁰ There have been some very large awards, but most awards cut the claims down drastically. Claims are made and based on the different standards set out in the BIT they are argued in as strong a manner as possible in the case. In the majority of cases, however, states prevail. Claims are frequently lost on the facts, rather than on a forced expansion of the meaning of a standard of protection. Examples under NAFTA include *Pope and Talbot*,¹³¹ in which the claimant made broad allegations of denial of fair and equitable treatment but received damages only for the abusive behaviour of Canadian civil servants in the conduct of the case. In a later case, *A.V. Gallo*,¹³² after extensive inquiry, the tribunal discovered that the claim was based on the fraudulent manipulation of company records. The awards in *Ethy*¹³³ and *S.D. Myers*¹³⁴ are based on a finding that the minister responsible preferred to close the border to imports and exports rather than regulate the conduct in Canada. The *Bowater*¹³⁵ case was settled by the Government of Canada because it was a case of expropriation without adequate compensation.

130 See Tim Hart, “Study of Damages in International Centre for Settlement of Investment Disputes cases” (2014) 3 Transnational Dispute Management 1 at 1 (“There have been 280 cases concluded at ICSID...the claimant only won more than 50% of what it claimed in around 12% of the reported cases and received between 20% and 50% of its claim in about 8% of the cases.”). See also ICSID, *The ICSID Caseload: Statistics*, *supra* note 29 at 28 (finding that among disputes decided by arbitral tribunal under the ICSID Convention and Additional Facility Rules in 2014, 30 percent of the awards declined jurisdiction, 35 percent of the awards dismissed all claims and 35 percent of the awards upheld claims in part or in full).

131 *Pope & Talbot Inc v Canada*, Interim Award, June 26, 2000 [*Pope*], online: <www.italaw.com/sites/default/files/case-documents/ita0674.pdf>.

132 *Gallo v Canada*, Award, 15 September 2011, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/disp-diff/gallo-11.pdf>.

133 *Ethy Corporation v Canada*, Preliminary Tribunal Award on Jurisdiction, 24 June 1998, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/disp-diff/ethyl-08.pdf>.

134 *SD Myers*, *supra* note 119.

135 *Abitibibowater*, *supra* note 119.

It must be pointed out that a number of NAFTA claims have been abandoned or have not been pursued and will thus be deemed to be abandoned in time.¹³⁶ It is one thing to make a claim, in effect to “try it on for size”; it is quite another to pursue it successfully. The more the arguments are forced and implausible, the less likely they are to succeed. Another factor militating against frivolous claims is their cost. ISA claims are complex matters and require a serious commitment of funds. Contingency funding of these costly cases does not appear to have occurred in cases against developed democracies but it would be an unwelcome development that is currently not prohibited by model BITs or any existing agreements.

The broad answer to the question as to whether all governmental policies are at risk must surely be answered in the negative. But it must be admitted that the wording of older BITs is very broad and general in scope. Developed democracies have been in the forefront of moves to tighten the language of BITs and FTAs; the most complex example is surely the EU-Canada CETA, which contains extensive guarantees against frivolous claims and overbroad reading of the standards of treatment. States can now weed out frivolous claims and issue a wider range of authoritative interpretations. How they will influence arbitrators can only be a matter of conjecture. The procedural guarantees of transparency added to NAFTA have not discouraged claims, but 31 claims in 20 years is hardly a flood, and the tighter wording of the newer agreements signed by Canada, the European Union and the United States may well have a dissuasive effect.¹³⁷

“ISA doesn’t provide fair and equitable treatment, full protection and security”

Critics frequently point to the decisions involving the failure to provide fair and equitable treatment as evidence of a vague and infinitely expanding standard that provides no certainty to governments. The recent *Bilcon* decision under NAFTA Chapter 11¹³⁸ is evidence of the uncertainty surrounding the meaning of fair and equitable treatment. This decision, made by a majority with a strong dissent, appears to depart from the understanding of this standard in previous NAFTA decisions, based on the 2002 note of interpretation¹³⁹ and most particularly the *Glamis*¹⁴⁰ case, fails to explain how state practice has evolved in recent years. Other decisions based on a rather expansive interpretation of fair and equitable treatment under other BITs around the world are also cited to justify this concern.¹⁴¹ Numerous academic critics have also focused on this issue.¹⁴²

Immense amounts of ink have been spilled over this question. NAFTA governments have intervened, and in CETA Canada and the European Union have adopted an even more restrictive definition of fair and equitable treatment,¹⁴³ as well as limiting full protection and security to physical protection.¹⁴⁴ Arbitrators have accepted that they are legally bound by these interpretations but have also suggested

136 See Foreign Affairs, Trade and Development Canada, “NAFTA – Chapter 11 – Investment: Cases Filed Against the Government of Canada: Notices of Intent Received and Current Arbitrations”, online: <www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/disp-diff/gov.aspx?lang=eng> for a list of notices of intent received and current arbitrations, previous arbitrations to which Canada was a party, as well as notices withdrawn or inactive. It is noteworthy that NAFTA contains no provision for the abandonment of claims. By contrast, the ICSID Convention contains articles on discontinuance (see arts 43, 44 and 45 of the ICSID Arbitration Rules, *supra* note 86).

137 In this regard, several agreements provide for additional procedural guarantees. An example of such guarantees can be found in the “frivolous litigation” clauses such as in article 41(5) of the ICSID Arbitration Rules, *supra* note 86 and art X.29 of Chapter 10 of CETA, *supra* note 5.

138 *Clayton*, *supra* note 119.

139 NAFTA Free Trade Commission, *supra* note 63, at (B).

140 *Glamis Gold Ltd v United States of America*, Award, 8 June 2009, online: <www.state.gov/documents/organization/125798.pdf>.

141 See e.g. *Merrill & Ring Forestry LP v Canada*, Award, 31 March 2010 [*Merrill*], online: <www.italaw.com/sites/default/files/case-documents/ita0504.pdf>; *Railroad Development Corporation (RDC) v Guatemala*, ICSID Case No ARB/07/23, Award, 29 June 2012, online: <www.italaw.com/sites/default/files/case-documents/ita1051.pdf>; *Occidental Exploration and Production Company v Ecuador*, ICSID Case No ARB/06/11, Award, 5 October 2012, online: <www.italaw.com/sites/default/files/case-documents/italaw1094.pdf>.

142 See e.g. Andrew Newcombe & Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International, 2009) at 272, para 6.23ff; Roland Kläger, “Fair and Equitable Treatment” in *International Investment Law* (Cambridge University Press, 2011) at 61ff; Graham Mayeda, “Playing Fair: The Meaning of Fair and Equitable Treatment in Bilateral Investment Treaties” (2007) 41:2 *Journal of World Trade* 273; and UNCTAD, *World Investment Report 2012: Towards a New Generation of Investment Policies* (Geneva: United Nations, 2012) at 139, online: <unctad.org/en/PublicationsLibrary/wir2012_embargoed_en.pdf> (“Some tribunals have read an extensive list of disciplines into the FET clause, which are taxing on any State, but especially on developing and least-developed countries; lack of clarity persists regarding the appropriate threshold of liability”).

143 CETA, *supra* note 5, Chapter 10, art X.9.

144 *Ibid* at Chapter 10, art X.9(5) (“For greater certainty, ‘full protection and security’ refers to the Party’s obligations relating to physical security of investors and covered investments.”).

that the customary standard can evolve over time and is not frozen.¹⁴⁵ In partial answer to this, the CETA parties have chosen an even more restrictive and limited definition of fair and equitable treatment. States have thus shown that they are capable of giving clear and firm direction. However, this does not solve the fact that there are now many different formulations of fair and equitable treatment in different BITs and FTAs and that claims are based on individual treaty texts and not on some amalgam of them all. Developed democracies thus have the capacity to control the meaning they give to fair and equitable treatment in the future, but it may be more difficult to restrict the meaning of past treaties. Some critics of the new language in CETA have already suggested that the power to interpret in CETA may be used to amend the actual meaning of the treaty text, or may be used by governments to issue interpretations of treaty language favourable to themselves, during the actual conduct of cases.¹⁴⁶

“Performance requirements are a serious constraint”

It is frequently argued by critics that the prohibition on the adoption of certain performance requirements in BITs constitutes an undue constraint on governmental choice and it is also alleged that the concept itself is too vague and unclear. Performance requirements have been invoked in several NAFTA Chapter 11 cases¹⁴⁷ but have been invoked more often in litigation under other treaties.

The first point to be made is that certain performance requirements that limit the sourcing of goods or limit their eventual sale have long been prohibited under the General Agreement on Tariffs and Trade (GATT);¹⁴⁸ they continue to be so under the WTO and are the object of the prohibition in the Trade Related Investment Measures (TRIMS) Agreement.¹⁴⁹ The policy concern must be with the broader definition of performance requirements found in a number of BITs¹⁵⁰ and FTAs,¹⁵¹ and the possibility of recourse to ISA in case the commitments are violated. The prohibition of performance requirements is more of a trade policy choice and less an investments issue: subjecting some actors in the market to certain conditions while allowing others to act with greater freedom is inherently discriminatory and an open invitation to create protectionist trade policies that have the effect of overriding general trade commitments. If states wish to pursue certain protectionist policies or feel the need to promote certain domestic industries, this is arguably best done by clear exceptions to the commitments of non-discrimination, which can be listed in the annexes to BITs and RTAs. To subject an incoming foreign investor to restrictive requirements as to sourcing and eventual sale, as a matter of general practice, is to deny the advantages the investor brings to the foreign market.

“Expropriation — especially indirect expropriation — can be interpreted too widely”

Expropriation of foreign assets has been a source of controversy and conflict for a very long time. It was the source of a number of major international disputes in the nineteenth and twentieth centuries; the pace of expropriations fell off sharply in the last years of the twentieth century but there have been a number of major incidents in recent years. The provisions requiring that expropriations be accompanied by prompt and adequate compensation are a central element of NAFTA Chapter 11

145 See e.g. *ADF Group Inc v United States* (2003), 6 ICSID Reports 470, ICSID Case No ARB(AF)/00/1 at para 179 [ADF], online: <www.italaw.com/sites/default/files/case-documents/ita0009.pdf>;

what customary international law projects is not a static photograph of the minimum standard of treatment of aliens as it stood in 1927 when the Award in the Neer case was rendered. For both customary international law and the minimum standard of treatment of aliens it incorporates, are constantly in a process of development.

146 See *Loewen Group, Inc v United States*, ICSID Case No ARB(AF)/98/3, Opinion of Sir Robert Jennings, 26 October 1998, esp at paras 29ff.

147 *Ethyl*, *supra* note 119; *SD Myers*, *supra* note 119; *Pope*, *supra* note 131; *Merrill*, *supra* note 141; *Mobil Investments Canada Inc v Canada*, ICSID Case No ARB(AF)/07/4, online: <www.italaw.com/cases/1225>; *ADF*, *supra* note 145; *Metalclad*, *supra* note 119; *Corn Products International, Inc v Mexico*, ICSID Case No ARB(AF)/04/1, online: <www.italaw.com/cases/345>; *Archer Daniels Midland Company v Mexico*, ICSID Case No ARB(AF)/04/5, Award, 21 November 2007, online: <www.italaw.com/sites/default/files/case-documents/ita0037_0.pdf>; *Cargill, Incorporated v Mexico*, ICSID Case No ARB(AF)/05/2, Award, 18 September 2009, online: <www.italaw.com/sites/default/files/case-documents/ita0133_0.pdf>.

148 See *Canada-Administration of the Foreign Investment Review Act* (1984), Report of the Panel adopted 7 February 1984, GATT Doc L/5504, 30th Supp BISD (1984) 140 [FIRA], online: <www.wto.org/english/tratop_e/dispu_e/82fira.pdf>.

149 *Agreement on Trade-Related Investment Measures*, 15 April 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1868 UNTS 186.

150 See e.g. art 8 of the US Model BIT (2012); art 7 of the Canadian Model FIPA (2004); and art 8 of the Norway Model BIT (2007).

151 See e.g. the *Free Trade Agreement Between Canada and Korea*, *supra* note 13, art 8; the *Free Trade Agreement Between the United States and Panama*, *supra* note 13, art 10.9; CETA, *supra* note 5, art X.5 (Chapter 10).

and virtually all BITs and trade agreements with investment chapters. NAFTA Chapter 11 innovated by covering acts “tantamount to” expropriation.¹⁵² Critics¹⁵³ view these provisions as hardening and giving credit to what is seen as an overly onerous and controversial international customary standard. They also consider that the concept of indirect expropriation is far too vague and that its use opens the door to abusive and even frivolous attacks on legitimate domestic regulation. Such claims have been made without success under NAFTA but with greater success in litigation under some other BITs and trade agreements.¹⁵⁴

A first point to be made is that restrictions on discriminatory and uncompensated expropriations have long been the object of customary international law. Arguably most BITs do not innovate with respect to the general international prohibition on discriminatory and uncompensated expropriation. What they do is provide an international remedy in arbitration. The essential question is thus whether ISA constitutes a better remedy than nineteenth-century gunboats and espousal of claims by states. Critics respond that domestic courts should be left to determine the legality of expropriation under the law of each state. Here the best is clearly the enemy of the good. Experience over centuries has shown that there are too many situations in which a government decides to act unilaterally and for a variety of reasons does not feel compelled or able to offer prompt and adequate compensation. Customary international law has developed over the years to deal with a genuine problem. BITs only add a new legal remedy; they do not create new law. In this area, as in all of the debate over ISA, there are two interests: those of states and those of foreign investors. Developed democratic states themselves are often torn between two imperatives: they do not like being sued, but they wish to ensure that their citizens investing abroad enjoy suitable protection from unfair treatment.

In one area, international investment law may well have contributed to the emergence of new law on expropriation in that it has helped to foster the emergence of a doctrine of “indirect” expropriation.¹⁵⁵ The closest analogy in domestic law (and a clear source of inspiration) is the doctrine of “regulatory takings” in US constitutional law.¹⁵⁶ The concept of indirect expropriation captures the reality of situations in which the value of a foreign investment is entirely nullified by new laws, regulations or decisions (or the failure to take necessary decisions) that make it impossible to proceed with the investment once begun. Capital is sunk and then the benefits cannot be realized. Such situations may arise out of confused and dysfunctional decision making, as well as more overt discrimination or the emergence of new regulatory regimes that have unforeseen consequences. Charges of indirect expropriation often raise acute questions of public policy and may be met with the defence from the state that it was dealing with a situation of necessity or extreme urgency. Arbitrators can be called upon to make difficult judgments upon state actions and these cases are often controversial and politically charged.

Due to the difficulties set out above, and due to a series of cases in which indirect expropriation has been invoked, a number of recent model BITs contain language restricting the scope of the concept.¹⁵⁷ The most recent attempt in an agreement is the annex to the article of CETA dealing with indirect

152 NAFTA, *supra* note 26, art 1110.

153 See e.g. Vicki Been & Joel C Beauvais, “The Global Fifth Amendment? NAFTA’s Investment Protections and the Misguided Quest for an International ‘Regulatory Takings’ Doctrine” (2003) 78 New York University Law Review 30; Elyse M Freeman, “Note – Regulatory Expropriation Under NAFTA Chapter 11: Some Lessons from the European Court of Human Rights” (2003) 42 Columbia Journal of Transnational Law 177; Howard Mann, “The Final Decision in *Methanex v United States*: Some New Wine in Some New Bottles” (2005), online: <www.iisd.org/pdf/2005/commentary_methanex.pdf>.

154 See e.g. *Saluka Investments BV v Czech Republic*, Award, 17 March 2006, at para 255, online: <www.italaw.com/sites/default/files/case-documents/ita0740.pdf> (under the Czech Republic-Netherlands BIT):

It is now established in international law that States are not liable to pay compensation to a foreign investor when, in the normal exercise of their regulatory powers, they adopt in a non-discriminatory manner *bona fide* regulations that are aimed at the general welfare. and *Suez, Sociedad General de Aguas de Barcelona SA v Argentina*, ICSID Case No ARB/03/17, Decision on Liability, 30 July 2010, at para 128, online: <www.italaw.com/sites/default/files/case-documents/ita0813.pdf> (under the Argentina-France BIT and the Argentina-Spain BIT); in evaluating a claim of expropriation it is important to recognize a State’s legitimate right to regulate and to exercise its police power in the interests of public welfare and not to confuse measures of that nature with expropriation.

See also generally, for a comparison of the expropriation provision under the NAFTA and the DR-CAFTA, Rachel D Edsall, “Notes – Indirect Expropriation under NAFTA and DR-CAFTA: Potential Inconsistencies in the Treatment of State Public Welfare Regulations” (2006) 86 Boston University Law Review 931.

155 See e.g. *Metalclad*, *supra* note 119; *Pope*, *supra* note 131; *SD Myers*, *supra* note 119; *Methanex*, *supra* note 119.

156 On the doctrine of regulatory takings in US constitutional law, see generally Stephen J Eagle, *Regulatory Takings* (LexisNexis, 2014).

157 The US Model BIT (2012), for instance, clarifies the meaning of the expropriation provision in annexes A and B. See also the Canadian Model FIPA (2004), Annex B.13(1); the Indian Draft Model BIT (2015), art 5, online: <https://mygov.in/sites/default/files/master_image/Model%20Text%20for%20the%20Indian%20Bilateral%20Investment%20Treaty.pdf>.

expropriation,¹⁵⁸ which seeks to narrow the definition considerably in comparison to some claims that have been made as to its scope. The EU-Singapore FTA¹⁵⁹ and the TPP leaked draft do something similar,¹⁶⁰ and it can be assumed that any TTIP text will follow the same pattern. Should the CETA pattern be more widely followed, the fears of abuse of this concept will not disappear but they should be considerably allayed.

“ISA is not needed: investors make their own choices and should live with them”

Some critics of ISA take the position that foreign investors should take domestic law as they find it. They choose to invest, hoping to make a profit, knowing what they are getting into and fully aware of the nature of the legal system with which they are supposed to deal. In short, foreign investors make their bed and should lie in it. Hence, ISA is not necessary: the BIT provisions, shorn of ISA procedures, should be sufficient.

The example generally given in support of this argument is Brazil, which has negotiated few BITs, only one of which has received formal approval, and yet there is much foreign investment in Brazil. It should be noted that MERCOSUR (the South American trading bloc) dispute settlement may apply to some investment disputes between partners to that RTA.¹⁶¹ But, as a general principle, the answer to this argument is found in the court systems and the corrupt administrations of a host of countries around the world. The whole purpose of ISA is to set up a body of standards of treatment that states agree to offer foreign investors and to ensure that these standards are applied in a neutral forum outside the inefficient, biased and possibly corrupt national courts. That corruption remains a serious problem around the world is clear from even a cursory reading of the Corruption Perception Index¹⁶² and similar indices of governmental behaviour in many parts of the world. ISA is, in a sense, only one example of the principle of diversity jurisdiction enshrined in the Constitution of the United States in 1789¹⁶³ to ensure that citizens of one state would receive justice in other states of the union. The 3,200 BITs that exist reflect the concern of governments that their investors need protection when investing in many developing countries. The general argument against ISA is very hard to sustain in the face of conditions in the courts of the majority of countries.

From an economic standpoint, it is hard to prove that BITs are essential to ensuring that foreign investment occurs and even harder to prove that no investments would be made in certain countries

158 CETA, *supra* note 5, Chapter 10, Annex X.11: Expropriation:

The Parties confirm their shared understanding that:

1. Expropriation may be either direct or indirect:

(a) direct expropriation occurs when an investment is nationalised or otherwise directly expropriated through formal transfer of title or outright seizure; and

(b) indirect expropriation occurs where a measure or series of measures of a Party has an effect equivalent to direct expropriation, in that it substantially deprives the investor of the fundamental attributes of property in its investment, including the right to use, enjoy and dispose of its investment, without formal transfer of title or outright seizure.

2. The determination of whether a measure or series of measures of a Party, in a specific fact situation, constitutes an indirect expropriation requires a case-by-case, fact-based inquiry that considers, among other factors:

(a) the economic impact of the measure or series of measures, although the sole fact that a measure or series of measures of a Party has an adverse effect on the economic value of an investment does not establish that an indirect expropriation has occurred;

(b) the duration of the measure or series of measures by a Party;

(c) the extent to which the measure or series of measures interferes with distinct, reasonable investment-backed expectations; and

(d) the character of the measure or series of measures, notably their object, context and intent.

3. For greater certainty, except in the rare circumstance where the impact of the measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non-discriminatory measures of a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations.

159 EU-Singapore Free Trade Agreement, *supra* note 34.

160 *Ibid* at Annex 9-A; TPP, *supra* note 7 at Annex II-B of the leaked investment chapter.

161 See UNCTAD, *Dispute Settlement: Regional Approaches: 6.2 MERCOSUR* (United Nations, 2003), online: <unctad.org/fr/Docs/edmmisc232add28_en.pdf>.

162 See the 2014 Corruption Perception Index, online: <<http://www.transparency.org/cpi2014>>.

163 US Const, art III(2).

without ISA. The studies done by the WTO do not seem to be conclusive,¹⁶⁴ and some recent OECD studies tend to suggest that they may make a marginal difference.¹⁶⁵ The economic case for ISA between developed democracies is even harder to make. Vast investments have been made between developed democracies without ever instituting BITs in general or ISA in particular. If developed democracies do not institute full ISA between themselves, little is likely to change in the existing pattern of foreign investment between them: trade agreements enhancing access and regulatory cooperation will do much more than ISA to promote trade and investment flows. The utility of ISA between developed democracies can only be argued as a marginally useful phenomenon and for other political and legal reasons.

“ISA may be a reasonable option in certain developed countries but is not appropriate between developed democracies”

A final argument, heard from time to time, is more selective. It is that while ISA may be useful in relations between developed, capital-exporting and developing, capital-importing states, it has no place in the economic relations between developed democracies. The move toward ISA in NAFTA was taken *per incuriam* and the further drift in this direction has been a serious policy mistake. This is a position that appeared to have been adopted by the Government of Australia for some years but now seems to have been abandoned.

It should be admitted that ISA is not the primary goal between developed democracies: market access for goods, services and investments is far more significant an objective than securing ISA between them. This being said, there are definitely situations arising in developed democracies where a law or administrative decisions can be adopted against which there are no remedies, as happened in the Newfoundland Bowater expropriation. Certain policies, such as the US “Buy American” rules, can be impossible to challenge before domestic courts. Parliamentary supremacy in the United Kingdom, Canada, Australia, New Zealand, and even in the United States, can provide cover for the adoption of laws against which there is no adequate domestic remedy. This is perhaps less true for EU law and Germany — but even Germany has exceptions in which foreign investors would have trouble challenging a domestic law violating the standards of a BIT. This seems to be true for most EU member states.¹⁶⁶ Post-communist countries of the European Union continue to have problems, either with new laws such as those curtailing the interest rates on mortgages denominated in foreign currency, or administration of laws for domestic political purposes, as in the Czech Republic.¹⁶⁷ The administration of justice is not thought to be of the highest standard in Bulgaria and Romania.¹⁶⁸ To the extent that this can still happen, causing problems for foreign investors, recourse to ISA is arguably justified.

The mere fact that governmental policies are challenged in ISA is surely of itself not a reason to reject it; governments may not like to have their policies challenged under ISA but this happens in domestic administrative law and constitutional law and EU law proceedings every day of the week and they live

164 See Axel Berger, Matthias Busse, Peter Nunnenkamp & Martin Roy, “More Stringent BITs, Less Ambiguous Effects on FDI? Not a Bit!” (2010) WTO, Economic Research and Statistics Division Staff Working Paper ERSR-2010-10, online: <www.wto.org/ENGLISH/res_e/reser_e/ersd201010_e.pdf>. See also Axel Berger, Matthias Busse, Peter Nunnenkamp & Martin Roy, “Do Trade and Investment Agreements Lead to More FDI? Accounting for Key Provisions Inside the Black Box” (2010) WTO, Economic Research and Statistics Division Staff Working Paper ERSR-2010-13 at 18, online: <www.wto.org/english/res_e/reser_e/ersd201013_e.pdf>.

We find strong evidence that liberal admission rules promote bilateral FDI. The existence and coverage of NT provisions in the pre-establishment phase enters our estimations highly significant and positive, independent of the method employed. By contrast, ISDS mechanisms appear to play a minor role.

165 For instance, the OECD reports that after participants to a roundtable on ISDS were asked whether ISDS and related investment treaties are serving development needs:

Of the 21...participants that responded to this question about whether investment treaties had helped countries attract foreign investment, 16 participants stated that they were neutral or didn't know, three agreed with the proposition and two disagreed.

One country noted, referring to the economics literature, that “available evidence does not suggest that ISDS provisions have any significant impact on investment flows”.

(OECD, “Government perspectives on investor-state dispute settlement: a progress report”, Freedom of Investment Roundtable (14 December 2012), at 12–13, online: <www.oecd.org/daf/inv/investment-policy/ISDSprogressreport.pdf>.)

166 See generally Marjolaine Roccati, *Le rôle du juge national dans l'espace judiciaire européen, du marché intérieur à la coopération civile* (Brussels: Bruylants, 2014) and Olivier Jacot Guillarmod, *Le juge national face au droit européen: perspective Suisse et communautaire* (Dossier de droit européen no. 3, Basel: Helbing & Lichtenhan, 1993); Amrita Narlikar, Martin Daunton & Robert M Stern, *The Oxford Handbook on the World Trade Organization* (Oxford: Oxford University Press, 2012) at 613ff.

167 See e.g. Lauder, *supra* note 101.

168 It is noteworthy that, in 2014, both these countries were ranked number 69 in the Corruption Perception Index (*supra* note 162) out of 175 countries (number 1 being the country with the lowest rate of corruption and 175 being the country with the highest rate of corruption).

with it. Is there really a difference due to the recourse to arbitration instead of courts? Many US FTAs posit that they do not grant rights exceeding those available under domestic law.¹⁶⁹ So long as this is generally true, and so long as arbitration is accepted as a genuine alternative to courts, is there really a tenable argument in principle?

There is a further major argument advanced in support of recourse to ISA between developed democracies: what would result if all developed democracies decided to follow Australia? Can there be one law for a few and another for most states? How would China respond to being designated as risky while Norway is not? Would this not destroy the whole edifice of BITs? Some might welcome this result, but it is necessary to remember that the interests of investors is the policy protected by ISA in BITs. States have created the network of 3,200 BITs and some 60 RTAs with investment chapters to protect the interests of their investors abroad. If abandonment of ISA between developed democracies would compromise that protection, would it be to the advantage of developed democracies? Arguably no, at least until domestic legal systems throughout the world can guarantee the same level of legal protection as that available in developed democracies.

“The only legitimate form of dispute settlement for investment disputes is interstate”

Some critics take the view that the mix of public and private law, coupled with the right of a private party to sue a state, is inherently illegitimate. From their perspective, all investment disputes should be submitted to intergovernmental procedures, either as set out in advance in treaties, or by way of ad hoc international proceedings. They point out that many BITs and investment chapters in RTAs actually contain interstate dispute settlement clauses and suggest that these procedures should be adequate.

The answer to this argument is that ISA was developed precisely to depoliticize investment disputes and to remove governments from the front lines. Espousal of claims is a slow and unsatisfactory process at best. The use of threats and armed force to obtain satisfaction in an investment dispute proved to be even less satisfactory in the nineteenth century and was abandoned.

The success of the WTO Dispute Settlement Understanding (DSU), an interstate procedure, is indeed remarkable. It has avoided politicization in the main, but this is due to the fact that all WTO members have a shared interest in respecting the common rules against non-discrimination of the WTO. A consensus exists to respect these rules, which even survived the stresses of the 2008 financial crisis.

PROPOSED SOLUTIONS AND ANALYSIS OF THE CHALLENGES FACING THE EFFORT TO REFORM ISA

Abolish ISA

This approach appears to be favoured by many critics of ISA who view it as fundamentally unfair to developing countries, and inimical to the democratic values and institutions of developed democracies, even though they invented the procedure. It would also be popular with the governments of Venezuela, Ecuador and Bolivia, which have been the object of a number of major arbitral claims — many of them successful.

This proposal, while popular among critics, poses insuperable political and legal difficulties. The beneficiaries of ISA, foreign investors who have placed trillions of dollars in developing countries and their governments, would be deeply opposed. The political impact of dismantling ISA would unsettle capital markets all over the world. Legally, the dismantling of 3,200 BITs and well over 60 investment

¹⁶⁹ See e.g. the preambles of the *Free Trade Agreement Between the United States and Panama*, *supra* note 13; the *Free Trade Agreement Between the United States and Colombia*, 22 November 2006 (entered into force 15 May 2012), online: <investmentpolicyhub.unctad.org/IIA/country/223/treaty/3388>; the *Free Trade Agreement Between the United States and Peru*, 12 April 2006 (entered into force 1 February 2009), online: <investmentpolicyhub.unctad.org/IIA/country/223/treaty/3376>; the *Free Trade Agreement Between the United States and Korea*, 30 June 2007 (entered into force 15 March 2012), online: <investmentpolicyhub.unctad.org/IIA/country/223/treaty/3226>. The preambles of these agreements all state in similar terms that: “foreign investors are not hereby accorded greater substantive rights with respect to investment protections than domestic investors under domestic law where, as in the United States, protections of investor rights under domestic law equal or exceed those set forth in this Agreement”.

chapters in RTAs and treaties such as NAFTA and the International Energy Charter would be close to impossible. The system is too deeply entrenched and the support from investors so strong that most governments would be totally unwilling to embark on such a course. The only means of dismantling the ISA system would be to do so incrementally, one new or renewed agreement at a time, or through the gradual overtaking of BITs by the extension of new ISA provisions in mega-regional RTAs.

Amend the TRIMS Agreement

One solution to the existence of a body of law dealing with investment would be to incorporate the principles of international investment protection law into the WTO TRIMS Agreement. This agreement currently deals only in a limited way with certain forms of performance requirements. This would bring investment law into the WTO, it would do much to unify the related fields of trade and investment law and would provide a single intergovernmental forum of dispute settlement under the WTO DSU. The latter feature would please those critics who consider that ISA should cut out the recourse of the private investor and replace it with intergovernmental dispute settlement.

If this could be accomplished, the compulsory and binding WTO DSU processes would apply between WTO member states. This would remove investment disputes from the private sphere, something that many critics would applaud. However the remedy sought, the invitation to the offending state to “withdraw the measure” would be infinitely more invasive than the action in damages under current ISA claims and would surely deeply displease the same critics. The difficulties of renegotiating a major new treaty in the WTO are similar to those of negotiating an MAI, and the difficulties of denouncing and phasing out 3,200 BITs and the investment chapters of many RTAs raise enormous problems. This solution, though it has some appeal, appears to be unacceptable or unattainable, given the current impasse of negotiations in the WTO. Finally, there is the fact that a few WTO member states are still not parties to investment agreements.

Internalize All Foreign Investment Protection Law

South Africa is engaged in a major experiment of seeking to do away with many of its BITs and replace them with a new, comprehensive domestic law governing foreign investment.¹⁷⁰ Part of this reform involves the return of authority over disputes with foreign investors to the domestic courts. After initial criticism focusing on expropriation, the South African government has now proposed extensive amendments of its Expropriation Act to protect the interests of expropriated foreign investors. In doing so, the draft bill proposes to weigh a range of factors.¹⁷¹ Many critics of ISA and BITs will applaud this initiative and it must be treated with great respect. In theory, if all states had legislation meeting the international standards set out on contemporary BITs, and if all had courts and administrative proceedings equal to those in a few developed democracies, the edifice of international investment protection law would serve no purpose.

The ISA world may be changing. However, the fact is that we have not yet reached the stage where most governments would be willing to tear down the edifice of foreign investment protection and the ISA system that goes with it. This approach may please some host governments but it is not yet evident that it is acceptable to capital-exporting governments in Europe, North America or China and Japan, and it is not self-evident that these governments are incapable of violating their treaties.

Revisit an MAI

Some critics of the current system of BITs and separate chapters in RTAs suggest that it is time to revisit the idea of an MAI along the lines of the multilateral agreement, which was drafted by the OECD and rejected by many states — both developed and developing — in 1999. It is argued that the time has come to bring order to the chaos of 3,200 BITs and an ever-growing number of RTAs and now mega-regionals containing investment chapters, as well as the International Energy Charter. A

¹⁷⁰ See *supra* note 18.

¹⁷¹ See e.g. Jeremy Cronin, “Jeremy Cronin explains reasons for Expropriation Bill” (17 April 2013), *Politicsweb*, online: <www.politicsweb.co.za/party/jeremy-cronin-explains-reasons-for-expropriation-b>; and “Parliament Calls for Comment on Expropriation Bill” (23 April 2015), online: <www.saes.binetlaw.co.za/public-enterprise/articles/parliament-calls-comment-expropriation-bill>.

single investment agreement would provide common standards and ensure a much more equitable procedural and substantive regime of law governing the treatment of foreign investment.

In theory, this is an appealing solution based on standardizing a single global approach to all the issues posed by foreign investment protection and ISA. But in a world where multilateral solutions are less and less appealing to states, and in a field where policy differences are so extreme, the chance of such a negotiation ever being contemplated by the international community and the chances of it succeeding are unfortunately nil at the present time.

Create a Global Arbitral Appeal Court

One proposal often heard from critics of the current ISA system is that there should be a universal international investor-state arbitral appeals tribunal having jurisdiction to hear appeals from all ISA awards. It is argued that an appeals tribunal would act very much as the WTO AB has done and would bring a much greater degree of uniformity and certainty to ISA decisions. The appeals tribunal would seek to approach like cases in like fashion, and to enunciate clear general principles as well as to provide a safety valve for those awards that are clearly wrong and should be overturned. In turn, arbitrators would receive guidance from the appeals tribunal in the future conduct of their proceedings in individual cases. A further argument in favour of an appeals tribunal is that a publicly appointed court would enjoy high prestige: it would receive deference from arbitrators and would inspire much more confidence from the public. It would be better able to deal with broad issues of public policy than individually nominated arbitral panels, and thus “get it right” when dealing with difficult cases.

Many critics of ISA see this approach as the right solution. They cite the remarkable example of the WTO AB in support. Unfortunately, this is a simplistic and untenable analogy. The WTO AB administers one body of law and has been seeking to bring order to this single field. Foreign investment protection law is not comparable, in that it is based on 3,200 BITs and an ever-growing number of investment chapters in RTAs. The single most invoked ISA procedure is that of the Energy Charter Treaty. Amending all these treaties to provide recourse to an appeals body is a task that would defy even the most enthusiastic reformer. It will not happen.

A further reason militating against the creation of a single appeals tribunal is that the protections set out in investment agreements vary considerably. Each treaty reflects the interests and objectives of the parties at the time of negotiation. On the surface, a number of standards resemble each other, but this resemblance can be deceiving. Words and context can differ greatly and it is not clear that having a single appeals tribunal, taking single approaches to multiple wordings, would reflect the intentions of the parties or be an improvement on the current system.

A further major difficulty, not discussed by critics, results from the fact that a considerable number of ISA proceedings are conducted under the UNCITRAL Arbitration Rules. Under these rules, should supervision be required, it would be provided by the domestic courts of the place of arbitration. If there were to be a global appeals tribunal, would it displace the reforming and supervisory jurisdiction of the domestic courts or would the appeal be allowed from the decisions of domestic courts? Either result would probably astonish critics of ISA, who regularly call for restriction of all complaints by foreign investors to domestic courts. In some countries, this might raise serious constitutional questions. There would thus be very complex questions of jurisdiction to be resolved.

On what grounds would an international appeals court be granted jurisdiction to hear appeals? Would the appeal be directly from the arbitral award or from the domestic courts? The very idea of an appeal is anathema to most modern conceptions of arbitration and the intervention of domestic courts is restricted to a narrow range of jurisdictional questions. Would an ISA appeal be based on a broader approach, allowing for appeals on a wide spectrum of questions of law and fact? What would be the powers of the court: to annul, to overturn in whole or in part, or to remit with orders to reconsider certain issues? Indeed, some would suggest that this should be a court of cassation, not a court of appeal. Would an ISA appeals court be able to do more than order damages and, like the WTO AB, be empowered to order the losing state to withdraw the measure? To pose these questions is to realize that a global ISA appeals court is not likely to be created in the near future.

It should be noted that the Canadian and US model BITs, for some time, as well as several recently concluded RTAs of the European Union, contain references to the creation of an appellate court at some point in the future, but no concrete steps have been taken.

Set up a Single ISA Court

A variant on this proposal is to suggest that all ISA claims be heard by an international tribunal set up by states. This court would enjoy high prestige, having been created by all states for a special purpose, and should be able to act like major courts in reconciling conflicting values. A variant on this proposal would be the requirement to choose all arbitrators from a closed list of arbitrators named in advance by governments.

Replacing all ISA ad hoc arbitral tribunals with a single global ISA tribunal is clearly a totally unrealistic and unacceptable concept. States have chosen to negotiate 3,200 BITs for a reason; they are not inclined to centralize everything on a single judicial institution and, if they did, it would be vigorously opposed by the community of foreign investors.

Strengthen Transparency in ICSID and Other Administering Agencies and Add an Appeals Process to All New Major Investment Agreements

Much could be done by administering agencies such as the Permanent Court of International Arbitration, the LCIA, the Stockholm Chamber, the American Arbitration Association, the ICC, the Hong Kong and Singapore chambers, China International Economic and Trade Arbitration Commission (CIETAC), etc., to increase transparency. ICSID has already amended its rules to increase transparency. The movement toward greater transparency by all administering agencies should assist in promoting public confidence.

It is also argued by some that the most practical approach is to take a number of ad hoc steps: strengthen the ICSID ad hoc committee process, review the rules of major administering bodies such as the ICC, LCIA, the Permanent Court of International Arbitration, etc.; and to adopt a policy of adding an appeals process to all new major agreements. This approach would catch a significant percentage of ISA cases and would increase the attraction of those procedures and institutions that did provide a genuine appeal from ISA awards.

A practical step that can be taken in the short term is to review and revise the rules governing the conduct of ISA proceedings by various administering bodies to ensure that a greater degree of transparency is provided. Thus, special rules for ISA proceedings could be promulgated by the American Arbitration Association, International Chamber of Commerce, LCIA, the Stockholm Chamber, the Hong Kong and Singapore arbitral bodies and CIETAC, etc.¹⁷² Whether this would be seen as desirable depends on the strategy of each body. The LCIA would probably not wish to do so, as it has always stressed the confidentiality of its proceedings. However, going beyond transparency changes by adding a full appellate process to any of these rules would probably be met with serious legal objections that this could only be done if the treaties themselves were amended prior to changing their own rules. The ICC, for instance, would doubtless point out that its court is designed to review all draft awards to ensure that the arbitration has been properly conducted. The ICSID has begun to play a similar role, reviewing draft awards before their issuance, albeit on an informal basis. The ICSID has already taken significant steps to reinforce transparency in ISA proceedings by amending its rules.¹⁷³

Transparency could be reinforced by administering agencies, but it is very doubtful that they could add an appellate process without treaty amendment. As a guarantee of greater transparency in proceedings under its own rules, in 2014 UNCITRAL adopted its new Convention on Transparency that, if widely adopted by states, will have a significant impact on UNCITRAL rules proceedings.¹⁷⁴ However, this new treaty does not set up any form of appellate process.

¹⁷² It is noteworthy in this regard that the Mauritius Convention that is now open for signature will bind the parties to the convention to apply the UNCITRAL Rules on Transparency (see *supra* note 88 and accompanying text).

¹⁷³ See *supra* note 89.

¹⁷⁴ See *supra* note 94.

One step toward a genuine appellate process that may be contemplated is the amendment of the ICSID Convention to change the existing ad hoc annulment committee process into an appeal or reference process. This could only be done by treaty amendment. The ICSID Secretariat floated this idea in 2004-2005.¹⁷⁵ Unfortunately, there was virtually no support among ICSID parties and the idea was dropped. Perhaps it is time to revive the idea, as it is the surest way toward adding an appellate or reference process that would apply to a significant proportion of all ISA cases. It cannot be said as yet that there is a groundswell of support but amendment of the ICSID Convention has the potential to provide an appeals process for a very large number of ISA awards.

Establish a Standing, Closed Roster of Arbitrators

It is sometimes argued that if states came together to name a small roster of highly qualified arbitrators from whose number all ISA arbitrators would be chosen, there would be much greater public confidence in the decisions rendered by panels of these arbitrators, rather than awards by individually selected arbitrators.

Arbitrators for the ICSID ad hoc committee are chosen from a relatively small group of very experienced and respected arbitrators and it has been suggested by some commentators that an appeals process might be founded on a roster of arbitrators rather than an appeals court. This proposal suffers from all the same difficulties as the creation of a standing appeals tribunal.

The concept of a standing, closed roster of arbitrators is also suggested as a partial answer to the question of public confidence in the ISA process. It is suggested that public confidence would be raised if all ISA arbitrations were decided by arbitrators chosen in advance by states from among a roster of arbitrators who could be trusted to understand the significance of their mandate to rule on both private and public interests. Like many of the suggestions from critics of the ISA system, this proposal is one sided. It may deal with the public concern, but it is not calculated to encourage confidence on the part of investors. It would almost certainly lead to challenges to the neutrality of members of the roster and refusal to name them, and calls to select arbitrators from off the roster, if not complete refusal to invoke arbitration. The essence of arbitration is to allow parties to each choose their arbitrator and for the two arbitrators to select a neutral chair of the tribunal. The proposed approach completely upsets this understanding of arbitration and would change the nature of the process.

Perhaps this change is needed to raise public confidence, and it should be noted that it seems to be the policy of the European Union since both the CETA and EU-Singapore RTAs provide for the constitution of a roster of ISA arbitrators.¹⁷⁶ Between these parties, the approach may work, but there is a history of difficulty among Canada, the United States and Mexico in naming members of the roster of interstate arbitrators for NAFTA Chapter 20 cases. The same difficulty may be encountered by the European Union, and the idea of having to submit all arbitrations to the friends of the president of a corrupt country will not be appealing to investors.

Perfect the Drafting of BITs and FTA Investment Chapters

Those supporting recent BITs and RTAs that incorporate ISA suggest that any problems that may exist — be they problems with existing procedures, vagueness in concepts or treaty terminology, or public confidence in ISA as a system — can all be resolved by more careful drafting of the treaties. This approach is clearly the policy currently followed by a number of governments of developed democracies. Starting from criticisms of particular decisions or treaty provisions, very considerable efforts have been made to revise model laws or standard terms in new treaties, with a view to resolving difficulties that have arisen in the past or to avoid problems that might arise in the future.

The text of the Canada-EU CETA is perhaps the best example. Both the general text and Chapter 10, on investments, contain a wide range of exceptions clauses designed to ensure that public policies of Canada and the European Union not be disturbed and that awards rendered under the ISA process respect the general public policy choices made by governments, unless their policies

¹⁷⁵ See ICSID Secretariat, *supra* note 106, concerning the previous attempt to amend the ICSID Arbitration Rules in this regard.

¹⁷⁶ See CETA, *supra* note 5, Chapter 10, art X.25 and EU-Singapore Free Trade Agreement, *supra* note 28, Chapter 9, art 9.21.

genuinely cross the line drawn by governments themselves. This includes: new drafting of the definition of standards; protection of public policy measures against allegations of failure to respect national treatment; new and more transparent procedures; broader and clearer exceptions clauses; and more explicit protection of environmental and consumer protection regulations, etc. Another example, albeit one subject to considerable uncertainty, would be the statement found in several US agreements that the investment protections do not exceed the rights enjoyed by litigants under domestic law.¹⁷⁷

More elaborate treaty language is the approach currently espoused by Canada, the United States and the European Union. It is the approach that is most likely to provide practical responses to the criticisms made of the ISA process. It also seems to be the approach currently adopted by many other states. UNCTAD reports that no less than 45 states were in the process of reviewing their bilateral agreements in 2014.¹⁷⁸ India recently announced the adoption of its new model bilateral,¹⁷⁹ Indonesia is engaged in a similar process¹⁸⁰ and South Africa is engaged in an even more radical reassessment of its bilateral agreements.¹⁸¹

If one takes the CETA text or the Canadian or US BITs as a model, it is clear that much can be done by this approach to enhance transparency and clarify substantive rules. In the CETA text, the public parties have substantially more control over the proceedings than in earlier BITs. They can weed out claims that are manifestly without legal merit at the start,¹⁸² they can challenge claims that are “unfounded as a matter of law,”¹⁸³ and various provisions¹⁸⁴ allow states to consult and to issue binding interpretations on “matters of interpretation.” As well, non-disputing parties may intervene in proceedings,¹⁸⁵ and they can consult on improvements to be made to the process or on the need for further interpretation of such standards as “fair and equitable treatment.”¹⁸⁶ The MFN standard has been restricted to substantive matters and does not extend to ISA procedures.¹⁸⁷ A number of important provisions provide protection of various public policy measures. Thus, the prohibitions on limiting market access do not limit the sovereign right to maintain various policies;¹⁸⁸ nonconforming laws are protected from the application of various standards if listed in the annexes to CETA. The provisions of the definitions in Chapter 2 exclude water in bulk from CETA commitments and the general exceptions chapter (Chapter 32) protects cultural industries and incorporates GATT-style exceptions in favour of health and environmental measures.¹⁸⁹

There are a number of very significant interpretive provisions that act to protect the regulatory powers of states. Chapter 32 significantly limits the effect of the national treatment standard.¹⁹⁰ The investments chapter (Chapter 10) contains a significant, new and restrictive definition of the fair and equitable treatment standard, limiting it to certain defined discriminatory acts,¹⁹¹ while the same article limits full protection and security to physical protection.¹⁹² Expropriation is the object of a full annex, which contains extensive definitions.¹⁹³ In particular, indirect expropriation is defined restrictively in the following terms:

For greater certainty, except in the rare circumstance where the impact of the measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, nondiscriminatory measures of a Party that are designed and

177 See *supra* note 169.

178 UNCTAD, *World Investment Report 2014*, *supra* note 21 at 126 (“at least 40 countries (and 5 regional organizations) are currently in the process of reviewing and revising their approaches to international-investment-related rule making.”).

179 See Indian Draft Model BIT, *supra* note 157.

180 See Bland, *supra* note 19.

181 See IISD, *supra* note 18.

182 CETA, *supra* note 5, Chapter 10, art X.29.

183 *Ibid.*, art X.30.

184 *Ibid.*, Chapter 10, arts X.27, X.42(3) and Chapter 32, art X.06(7).

185 *Ibid.*, art X.35.

186 *Ibid.*, art 42(3)(d).

187 *Ibid.*, art X.7(4).

188 *Ibid.*, art X.4.

189 *Ibid.*, Chapter 32, art X.02.

190 *Ibid.*

191 *Ibid.*, Chapter 10, art X.9.

192 *Ibid.*, art X.9(5).

193 *Ibid.*, Annex 11.

applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations.

Finally, several provisions codify the various principles of transparent and open proceedings that they both defend within their own judicial systems and internationally.¹⁹⁴

The net effect of these provisions, some entirely new, others expanding on NAFTA provisions or taken from model BITs, is to provide extensive protection, if not sometimes total exemption, of a range of regulatory measures and policies. It must be noted that some of these exemptions and interpretations rely on provisions outside the investment chapter.

Subject to the interpretative pitfalls alluded to above, the decision to expand the scope of explicit exemptions and clarifications is understandable. In the face of the NAFTA case experience, and in the face of public criticism of the ISA process, this approach constitutes the most effective response readily available to both parties.

In response to these criticisms, it may be said that the exemptions and exceptions are so pervasive and complex that one must ask whether there is a risk that they may be self-defeating. The early BITs were no more than 10 pages in length, often shorter. The Canadian FIPA, on which this is modelled, is 45 pages in length. CETA Chapter 10 has 38 pages and is supplemented by provisions elsewhere in the text. The parties have gone far toward exhaustively protecting their right to regulate in the public interest by defining, exempting or protecting the exercise of these powers. But have they gone too far? Like the enthusiastic common law draftsman seeking to cover every eventuality, they may well have created an overly complex text that may pose as many problems of interpretation as it solves. It is impossible to envisage every eventuality and with a very complex text there may be a danger that general principles may be lost in the details and arbitrators may be tempted to assume that what was not explicitly covered is not subject to the disciplines of the agreement.

Give States More Power to Control ISA Procedures, Eliminate Bad Cases and Interpret Meaning of Vague Standards

A further development in response to criticisms of ISA has been to expand the controls that states exercise over the process. This approach is reflected in the Canadian and US model BITs and even more fully in the current text of CETA as well as the EU-Singapore FTA. The CETA text allows the parties to eliminate frivolous claims¹⁹⁵ at the very inception of a claim, as well as allowing the parties to put an end to claims that have no merit.¹⁹⁶ Several provisions allow the parties to consult and to issue binding interpretations of the text. In this way, the European Union and Canada expect to be able to ensure that the thrust of claims and the interpretations of arbitrators remain faithful to the text.

These provisions have not been without controversy and private interest groups have already begun to express the fear that states may intervene during the conduct of proceedings to limit the meaning of a particular standard or even to act in a manner tantamount to amending the treaty.¹⁹⁷

Abolish the ISA System or Exempt Developed Democracies from ISA

Australia, at one point in the recent past, appeared to be adopting a general position hostile to any recourse to ISA in any of its BITs. Some critics of the system suggest that the best approach to the problem would be to exempt at least all developed democracies from recourse to ISA. On the assumption that ISA is contrary to democratic principle and that the mistreatment of foreign investors should be dealt with exclusively by domestic courts under domestic law, it is argued that the only proper solution for developed democracies is, as a minimum, to withdraw from ISA

194 *Ibid*, Chapter 10, art X.33(1) (“Transparency of Proceedings”). See also article X.34 (“Sharing of Information”) of the same chapter.

195 *Ibid*, Chapter 10, art X.30.

196 *Ibid*, Chapter 10, art X.29.

197 See Nikos Lavranos, “Comment: Turning the tide on deteriorating EU investment protection standards after Lisbon” (24 February 2015), online: <www.borderlex.eu/comment-turning-tide-deteriorating-eu-investment-protection-standards-lisbon/>. See also Nikos Lavranos, “The lack of an FET-standard in CETA” (McGill University-Queen Mary University of London Conference on Investment and ISDS in CETA, Montreal, 1 November 2014), online: <www.mcgill.ca/fortier-chair/files/fortier-chair/2014_ceta_lavranos_nikos.pdf>.

commitments between themselves and to conclude no more *inter se*. Opponents of ISA would doubtless prefer the whole system to be dismantled but as a minimum it should not be used between developed democracies. This would imply eliminating the existing ISA provisions from CETA,¹⁹⁸ and seeking to withdraw Canada and the United States from the requirements of Chapter 11, P, of NAFTA. Switzerland and Japan would have to do the same for their 2009 FTA.¹⁹⁹ The BITs between EU member states would have to be amended to remove the ISA provisions, as well as Canada's and the United States' BITs with several EU member states of Central Europe and the Baltic. ISA would not be incorporated into the future TTIP and could not be used against the United States and Canada under the future TPP.

If abolition is impossible, as suggested above, would it be possible to exempt developed democracies from recourse to ISA *inter se*? If one excepts the 190 BITs between Western and Eastern member states of the European Union — concluded in the Communist era — the numbers are not large. There are several recently concluded Canadian BITs with the same states replacing their Communist-era BITs; Japan and Switzerland have a recent FTA that includes ISA; Korea has recently signed an agreement with Australia²⁰⁰ and it also has several with EU states concluded when Korea was still a developing capital-importing state.²⁰¹ NAFTA and the International Energy Charter involve developed democracies among the parties as well as others. It is clear that many citizens feel uncomfortable with ISA, for reasons canvassed above, and it is equally clear that their governments do not relish being sued. There is strong resistance in Europe to ISA with the United States in the TTIP, and in Japan in the TPP, for the same reason. There have been calls for removing ISA from the CETA text before the final process of ratification begins.²⁰²

Exempting ISA between developed democracies seems the obvious course of least resistance. But is it? Has the process not already gone too far to turn back? In the first place, there is the issue of the validity of the argument of the impropriety of ISA in developed democracies. Arbitration generally is accepted. Is ISA so very different? Some hold this view due to the mix of private and public issues in ISA for determination by arbitrators instead of courts. Second, there is the fact that situations exist where democratic governments have acted in a discriminatory fashion against foreign investors. No government is perfect. We have seen at least two acts of flagrant discrimination and one of unabashed expropriation without compensation in Canada, and not all the governments of the European Union stand high on the Global Corruption Index. Europeans and Canadians have some cause for worry. But the worry is marginal and arguably *de minimis*. Both sides could live together comfortably without recourse to ISA. At a minimum, they should be able to stop concluding ISA agreements between themselves.

But if developed democracies do decide to stop concluding ISA agreements *inter se*, they will still be faced with three serious problems: the agreements already in force; the agreements in force or under negotiation involving many third states as well as developed democracies; and the reaction of all other states to a new policy of developed democracies of refraining from ISA *inter se*, but maintaining the 3,200 existing BITs and RTAs and the International Energy Charter with all the others.

These problems would not be easily resolved. How would Canada and the United States remove themselves from NAFTA Chapter 11, Part B, with the consent of Mexico and without having to renegotiate many delicate questions? How would the democracies that are parties to the International Energy Charter exempt themselves from ISA *inter se* while maintaining their obligations vis à vis all the other parties? Would this not involve renegotiation of a vitally important international treaty with the attendant uncertainties of such a negotiation? Simply renegotiating treaties is a slow and complex business involving officials who are already busy negotiating new agreements. But it could

198 See above regarding the position of the German minister of industry and the French socialist party.

199 *Japan-Switzerland Economic Partnership Agreement*, *supra* note 54.

200 *Free Trade Agreement Between Australia and Korea*, *supra* note 48.

201 See e.g. *Treaty Between Korea and Germany Concerning the Promotion and Reciprocal Protection of Investments*, 4 February 1964 (entered into force 15 January 1967), online: <investmentpolicyhub.unctad.org/Download/TreatyFile/1351>; *Accord entre le Gouvernement de la République française et le Gouvernement de la République de Corée sur l'encouragement et la protection des investissements*, 28 November 1977 (entered into force 1 February 1979), online: <investmentpolicyhub.unctad.org/Download/TreatyFile/1239>; *Agreement Between the Government of Denmark and the Government of Korea Concerning the Encouragement and the Reciprocal Protection of Investments*, 2 June 1988 (entered into force 2 June 1988), online: <investmentpolicyhub.unctad.org/Download/TreatyFile/1011>.

202 See *supra* note 32.

be envisaged if developed democracies were willing to pay the price. Bilateral commitments to ISA between developed democracies are not yet numerous, if one assumes that the European Commission will succeed in its quest to have EU member states abandon their 190 BITs with each other, inherited from days before the adhesion of Eastern European states to the European Union. Canada is planning to abandon its BITs with several EU states when CETA enters into force. But the problem of RTAs and the Energy Charter is much more serious. ISA provisions in the Energy Charter have been used more than any other ISA procedure. They have been used only twice against Germany but have been invoked against several other EU member states and by EU member states. This is not a treaty that the European Union can safely compromise.

Further complicating the situation is the fact that ISA is part of the CETA and EU-Singapore trade agreements. Would Canada agree to withdraw the ISA provisions from CETA at the last minute? Is Singapore a developed democracy in the eyes of the European Union and, if it is, how would Singapore respond to the idea of eliminating its ISA protections for its investors in the European Union? Even more delicate is the fact that ISA clauses are said to be in the TTIP and the TPP texts. Would the United States agree to withdrawing ISA from the TTIP draft text and would it and the other parties to the TPP negotiation be willing to restrict the application of ISA to actions against the non-democratic developing countries who form the majority of the negotiating partners? Perhaps solutions to these questions could be found, but it would not be easy.

The final question in this regard concerns the reaction of the non-democratic developing states of the world, which comprise by far the greatest number of states. How would they respond to being classified as unworthy of an exemption from ISA? The reaction is likely to be very negative and might well compromise the security placed in existing BITs by capital-exporting states, to the detriment of their foreign investors.²⁰³ For better or for worse, however uncomfortable the people and governments of developed democracies may be in the face of ISA action against them by foreign investors, and however tempted they may be to abolish ISA *inter se*, the reaction of the rest of the world to such a gesture cannot be ignored.

Limit ISA Claims to Situations Where There Are Demonstrably No Domestic Remedies

A refinement on the total abstention from recourse to ISA would be to add a clause to all existing and future BITs and RTAs requiring that there could be no recourse to ISA procedures unless it could be proven that no domestic remedy exists, thus ensuring the primacy of domestic courts and domestic remedies as desired by many critics of ISA.

For the reasons outlined at various points above, opening and renegotiating ISA commitments in existing BITs and RTAs with investment chapters would be a daunting, if not insuperable, task and it does not appear to be a viable option. The problems it would create would be far greater than the problems it would resolve.

What would be possible would be to add such a clause to all new BITs and RTAs. This could be added to all future agreements and could apply to agreements under negotiation, to agreements not yet in force and which remain controversial, such as CETA. It would answer the concerns of many critics that domestic courts are bypassed by ISA proceedings and would stress the primacy of domestic law and the responsibility of all states to see that their investment protection commitments are fully implemented.

This clause would not be without its difficulties and its own critics. It looks very much like the “exhaustion of local remedies” rule, which most BITs eliminate. Critics would point out that the avoidance of domestic courts is very much the object of ISA proceedings. They would also point out that the question of the existence of the remedy before domestic courts under domestic law, or of its adequacy, would become the source of much legal difficulty for private foreign investors and doubtless would be the source of controversy and perhaps conflict between states. States would have to decide whether it is worth the trouble of responding to the critics of ISA by creating new problems for foreign investors by significantly removing the protection they currently enjoy under BITs.

203 This question is examined in a separate paper by Hugo Perezcano.

At a Minimum, Apply this Rule to Developed Democracies

A further refinement on this approach would be to restrict its application to BITs and RTAs between developed democracies.

A refinement on the solution to restrict ISA to situations where no domestic remedy exists would be for developed democracies to adopt this approach for their future investment protection commitments *inter se*. This may well be the only way to respond to critics of the TTIP or to critics of the current CETA text. It would be seen by critics as a partial but sensible response that goes to the heart of most major criticisms. It would be much harder to apply to the TPP. Retroactive application to all existing agreements, except perhaps the BITs between EU member states, raises all the difficulties outlined above.

Abolish ISA and Move to Interstate Dispute Settlement

Some critics of ISA argue that all investment disputes under investment treaties should be resolved strictly between states. Treaties are made by states, and treaty disputes are inherently interstate and international disputes to which private entities and persons should not be a party. Some critics add that all investment disputes should go before the WTO DSU.

ISA was developed to deal with the deficiencies of dispute settlement under public international law. At international law, no state can be compelled to submit to formal dispute settlement, provided it respects its obligations of “pacific settlement” under the United Nations Charter. There is thus a fundamental problem with interstate proceedings. These problems can of course be remedied by treaty, and many trade and investment treaties have some limited form of compulsory interstate dispute settlement. The WTO DSU is, in effect, compulsory and binding in trade disputes and a very limited number of investment-related trade disputes.²⁰⁴ The question is whether intergovernmental dispute settlement responds to the needs of foreign investors. Arguably it does not. Investors have no right to dispute settlement. They must convince their government to espouse their case. Investors are not party to interstate disputes and cannot frame the question or control the proceedings. States will always weigh the political advantages and disadvantages of taking an international action against another state; in general, states are very reluctant to do so. Those states, such as China, that used to include only interstate dispute settlement have moved steadily toward the general recourse to ISA in their more recent treaties.

A further complication lies in the nature of the remedy sought in ISA as compared to interstate dispute settlement. The claim for damages resulting from violation of a standard involves bringing extensive factual economic and commercial evidence. It is not clear that this evidence can be easily brought by a government on behalf of their nationals.

This approach would not be viewed as a useful answer to the criticisms against ISA by foreign investors and would surely be opposed by them. The whole purpose of ISA is to avoid the political uncertainty and arbitrariness of intergovernmental procedures. States have reasons for espousing a claim (or refusing to do so) that may have little to do with the interests of foreign investors. Intergovernmental procedures are long, uncertain and not likely to provide the results of ISA. Intergovernmental procedures are best limited to questions that reflect a clash of governmental interests. With the exception of the WTO DSU, where states have a clear interest in clarifying WTO law and in asserting their individual and collective interests before the Dispute Settlement Body, the most successful international proceedings in recent years, such as those before international human rights courts or before the CJEU, have all involved granting a private right of action to private actors.²⁰⁵ To revert to a purely interstate system would effectively deprive foreign investors of both the procedural but also the substantive rights that they can currently exercise under ISA. The approach would kill international investment law: a solution that would perhaps please some critics, but surely not all, and surely not the defenders of the current system.

204 See e.g. *FIR*, *supra* note 148.

205 See generally Karen Alter, *supra* note 73.

THE WAY FORWARD?

This paper has examined the opportunities available to developed democracies with respect to the reform of the law and practice of ISA. Clearly, a number of reforms have been undertaken by states such as Canada as a result of their experience with ISA litigation. Many other avenues of reform are available. These avenues pose significant challenges and some are arguably more likely to succeed than others, but the fact of a challenge is no reason to face it.

It is hoped that this paper, and the full range of papers in the Investor-State Arbitration project, will provide a useful basis for discussion of the options now available to Canada and other democracies around the world.

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