

Amendment from Group I on ISDS (REX/411)

Delete whole Opinion and replace as follows:

1. Conclusions and Recommendations

1.1 Foreign Direct Investment (FDI) is an important contributor to economic growth and jobs. Companies that invest in another country are ipso facto taking a specific risk, but foreign contractors need to be protected against disproportionate and abusive treatment by the host State where they have invested, such as through direct expropriation, discrimination on grounds of nationality and unfair and unequal treatment when compared with domestic investors. A neutral disputes mechanism is important. Investments are often very long term and political circumstances in host States can change.

1.1.1 An International Investment Agreement (IIA) between two states (or Regions) involves international law. To be effective that needs an effective, balancing, international disputes settlement mechanism.

1.1.2 In most IIAs however the disputes settlement mechanism puts together individual companies and the host state through the Investor to State Disputes Settlement (ISDS) Procedure¹. ISDS is retrospective in character. Unlike the WTO Disputes Settlement Procedure, if a state loses a case only payment of compensation is involved. It does not need to repeal the relevant legislation. Investment is not a WTO competency, being dropped from the Doha Round agenda in 2003.

1.2 The EU is both the largest provider and recipient of international investment. Investment is a core interest for EU business, including SMEs. The Committee therefore welcomes the Commission position² that ISDS is:

- *An important tool for protecting investments and therefore for promoting and securing economic growth in the EU*
- *An effective way of enforcing the obligations our trading partners agree on with our investors when they sign investment treaties.*

1.2.1 A Business Round Table organised by the EESC Employers' Group on the Transatlantic Trade and Investment Partnership, TTIP, concluded³ that: *"An international agreement such as TTIP should create the right conditions to attract a high level of future investment in the transatlantic market. This includes granting ample access and non-discriminatory treatment for investors on both sides and improving the current framework for IP, including ISDS by making it more accessible to SMEs and striking a proper balance between investor rights, the right of states and local authorities to regulate in the public interest"*.

1.3 The EU-Canada trade agreement (CETA), yet to be ratified, includes an extensive investment protection chapter including provision for ISDS. This, together with the investment chapter in the EU-Singapore Free Trade Agreement⁴, is the first ever investment agreement negotiated by the EU since it gained competency for investment under the Lisbon

¹ Provision for ISDS is found in some 93% of the more than 3,250 IIAs signed to date, although the procedure has only been used in under 100, less than 3%.

² EC – Factsheet on ISDS – Paragraph 2 – 3/10/2013.

³ EESC Business Round Table – Common Declaration on TTIP, 16/12/2014.

⁴ Also still to be ratified, and subject to legal challenge in the ECJ as to whether it is a ‘mixed’ agreement and therefore needing approval by all MS Parliaments

Treaty in 2009. This has gone a long way to address outstanding concerns, but ISDS needs to evolve further.

1.4 Apart from "the principle of Most Favoured Nation" (MFN), and the cover normally included by the Commission to deal with compensation in cases of war, revolution and so on, the Committee urges that investor protection under an IIA and therefore open to the use of ISDS, must be restricted to cover the four substantive protections, namely

- Not to discriminate on grounds of the nationality of an investor
- A minimum standard of treatment, usually described as "fair and equitable"
- Prompt, adequate and effective compensation when expropriation occurs (not discriminatory and with due process)
- Allowing transfer of funds related to the investment

1.5 Over time a number of real and perceived abuses have arisen through the use of ISDS and these need to be addressed. ISDS needs to be updated. The Committee welcomes the four areas for further study on investment protection and ISDS identified by the Commission in January 2015 as a result of its public consultation on investment protection and ISDS in TTIP, following its inclusion in the mandate for the negotiations given unanimously by the Member States.

1.5.1 These covered

- The protection of the State's right to regulate
- The establishment and functioning of arbitral tribunals
- The review of ISDS decisions through an appellate mechanism
- The relationship between ISDS and domestic judicial systems

1.5.2 The Committee considers due protection of the **State's right to regulate** to be essential, and any remaining ambiguities removed. As stated in the Committee's Opinion on TTIP⁵, it is "*essential that any ISDS provision proposed in the TTIP does not hinder the ability of the EU Member States to regulate in the public interest*". Previous IIAs have been primarily drafted with the need to protect investments. Both CETA and the Singapore Agreement have tightened key definitions to avoid unwarranted interpretations and specifically refer to the right to regulate in the preamble to each agreement. The EESC considers that this should now be included in the body of the relevant text, as a specific Article of any such agreement.

1.5.3 It is essential that **arbitrators on ISDS tribunals** must be fully impartial and not open to conflicts of interest. The Committee urges that all arbitrators must be chosen from a roster pre-established by the Parties to the relevant agreement, and that clear qualifications are established for such arbitrators, notably that they are qualified to hold judicial office and have proven expert knowledge in the relevant fields of international law.

1.5.4 An **appellate mechanism** is also essential – a legal process without a right of appeal is rightly very rare, although this exists in current IIAs. The EESC notes reference was made to an appellate mechanism in the original TTIP negotiating directives. Design of such a mechanism will be critically important, including the methods how members are designated, their qualifications and remuneration, together with any time limits to be applied. It should cover errors of law and errors of fact. Early consideration should be given as to whether a bilateral mechanism could be made multilateral, perhaps modelled on the WTO Appellate Body. Any such mechanism will involve extra costs, but that should be taken into account.

⁵ Opinion REX/390 Transatlantic trade relations and the EESC's views on an enhanced cooperation and eventual EU-US FTA. June 4th 2014. Rapporteur: Jacek Krawczyk, Co-rapporteur: Sandy Boyle. (<http://www.eesc.europa.eu/?i=portal.en.rex-opinions.32281>)

1.5.5 The relationship between **ISDS and domestic judicial systems** will be harder to resolve. IIAs are international agreements and domestic courts do not necessarily have the competence to interpret matters of international law. Even the best system can falter, but double claims should be prohibited. Either potential litigants should make a final choice at the start of proceedings, or lose the right to go to domestic courts as soon as they turn to ISDS.

1.6 A multilateral, **International Court** is the longer term answer. This needs to be developed in parallel with the development of ISDS in TTIP and elsewhere. It is imperative that some form of international investor protection remains whilst such an international body is negotiated and established.

1.6.1 It is important to ensure critical mass for the establishment of an International Court as the longer term objective for investment dispute settlement. The widespread acceptability of such an international appellate mechanism is likely to stem from it being set up through consensus, which should deal with potential related problems that all new international institutions, including the International Criminal Court, face.

1.6.2 The EESC cautions against the suggestion that, as all "G7" members are currently involved in IIA negotiations, these start to develop an International Court separately by themselves. Critical mass can only be achieved if a much wider spread of countries involved from the onset, and the door is left open for others to join as and when they are interested.

1.6.3 In the meantime, the EESC recommends the EU and the US to engage on a bilateral investment dispute settlement mechanism in the TTIP.

2. Background

2.1 The Committee notes that if two countries desire to promote economic relations with each other through an International Investment Agreement (IIA), each will promise the other that they will guarantee certain levels of treatment to investors and investments from the other country. These promises, willingly entered into, then need to complete full domestic ratification processes. They do not in any way prioritise corporate interest over the right of governments to so regulate. In the interests of the rule of law governments do however need to be held to the guarantees they give.

2.2 The Committee recognises that, although negotiating States look to include provisions to protect their own companies against discriminatory actions of trade partners, it is unrealistic for an aggrieved company to expect that any dispute should automatically be taken up at State-to-State level, thus raising the issue to a political or diplomatic level.

2.2.1 If companies were to rely on the EU to take disputes up on a State to State basis, only a very few could be so pursued, and smaller companies would be less likely to have their voices heard. It is unlikely that there would be many cases between two mature democratic legal systems, but if State to State Disputes Settlement Procedure were to become the norm, the number of potential cases would be bound to rise, with major resource implications for States.

2.2.2 As Commissioner Malmström herself has pointed out⁶ in connection with the TTIP negotiations, international law cannot be invoked in US courts, and no US law prohibits discrimination against foreign investors. In other countries, domestic courts may be less trustworthy.

⁶ EP, 18 March

2.2.3 Investment is not identical to trade. In a trade dispute the onus is clearly on a state to take the lead. Such disputes are likely to involve a class of production, such as bananas, solar panels or textiles: dumping is a key WTO DSP issue.

3. The evolution of ISDS

3.1 Although the overall number of ISDS ⁷cases remain small, its use has grown substantially since 2002. This is proportionate to the increase in overall FDI, which globally by 2013 had exceeded US\$25tr. European investors have launched some 50% of all claims since 2002. A sizeable number of these have been launched by smaller or specialist companies ⁸. It is important that any reformed ISDS procedure must be made more accessible to SMEs.

3.1.1 Of the 356 known cases that have been concluded, 25% were resolved in favour of the investor, and 37% in favour of the state. The rest were settled ⁹.

3.2 Due to issues - both perceived and in reality - arising from the outcome of a number of ISDS cases worldwide, including a number that are still on-going, an increasingly notable part of public opinion in the EU, led by unions, NGOs and other organisations, has become concerned about its use, with opposition growing to an investment chapter and ISDS in TTIP.

3.3 Without reform of ISDS, and the inclusion of an Investment Chapter in TTIP, the Committee notes that previous arrangements as found in the 1,400 Bilateral Investment Treaties (BITs) negotiated by individual Member States (with the exception of Ireland), and those in particular previously reached by nine Member States with the US, would of course still stand and remain valid.

Reason: to take the argument forwards, not back
May 2015

⁷ 610 cases by the end of 2014

⁸ The Stockholm Chamber of Commerce reports that out of some 100 cases completed between 2006 and 2011, some 22% were undertaken by SMEs; the BDI also report that some 30% cases undertaken by German companies were from SMEs

⁹ EC Factsheet on ISDS, 3 October 2013