



November 10, 2015

**TABC Position Statement on European Commission's Draft Text on Investment Protection and an Investment Court System in TTIP**

On 16 September, the European Commission introduced a draft text on investment revising its model of investment protection and creating an investment court system to be included in the Transatlantic Trade and Investment Partnership (TTIP), as well as in all other ongoing and future EU trade negotiations. It includes new substantive provisions on investment protections as well as the establishment of a new investment court system.

The European Commission's text follows a [Public Consultation process](#) and previously released Concept Paper responding to the increased criticism of the traditional Investor-State Dispute Settlement (ISDS) process. The provisions depart from the investment chapter in the EU-Canada Comprehensive Economic and Trade Agreement (CETA) agreement.

**General Assessment**

The Trans-Atlantic Business Council (TABC) supports the Commission's efforts to modernize and improve existing investment agreements. However, TABC has serious concerns about parts of the proposal that will likely weaken investor rights, including substantive provisions on the right to regulate, fair and equitable treatment, and expropriation. In addition, we question the necessity and functionality of the Commission's proposed investment court.

TABC notes that many of the proposed revisions to the process have already been made in recent updates of the International Centre for Settlement of Investment Disputes (ICSID) rules and procedures. ICSID already provides an impartial, neutral forum for investors and States to bring investment disputes so TABC questions the need to depart from the ICSID model and create a new forum. We acknowledge that the EU cannot be a full member of ICSID as the U.S. or EU Member States are, but the EU Commission should determine how the EU can participate in ICSID to a larger extent.

Our concerns were already submitted in the initial consultation, but unfortunately the current proposal alleviated only very few of these concerns. TABC hopes the European Parliament and the Council take these views into consideration during the internal discussion process before a final proposal is presented to U.S. negotiators.<sup>1</sup>

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<sup>1</sup> This response corresponds with the comments TABC submitted to the European Commission during the public consultation on investment protection and investor-to-state dispute settlement (ISDS), as well as TABC's Response to the Commission's Concept paper.



Strong protections for investors are an integral part of any modern investment treaty. These protections greatly increase legal certainty and minimize risk when an investor is assessing whether to invest in a particular foreign market. Investor protections increase legal certainty and minimize risk when an investor is assessing whether to invest in a particular market.

The TTIP negotiations were launched with the ambition to set a gold standard trade and investment agreement which would set a norm for the 21st century. For this reason the investment provisions in TTIP should not be narrowly defined but, instead, should leave sufficient flexibility to adapt to the fast changing realities that exist in today's global trade and investment system.

Time and again, European investors have benefitted from meaningful investor protections – indeed, European investors have historically filed more than half of investment arbitration claims. It is vital that such protections, which already account for the right of governments to regulate and enact reasonable non-discriminatory regulations, are not diluted.

European and American investment represents the majority of the world's foreign investment. There is thus a transatlantic common interest in ensuring that TTIP supports a secure and stable investment climate, protected by the rule of law and clear, transparent standards. This is critical not only for the investments to be made under the auspices of TTIP, but also to set high standards for future investment agreements.

### **Substantive Provisions**

#### ***Right to Regulate (Section 2, Article 2)***

##### **Summary of draft text proposal**

The right to regulate is explicitly stated in the text as an article, rather than in the preamble as it is in CETA. The definition of right to regulate in the draft text is broader than the Commission's previous proposal for services, investment and e-commerce text in TTIP.<sup>2</sup> The proposed text also makes clear that States are able to change their "legal and regulatory framework", even if these changes harm investors. Further, the text cites specific areas protected by the right to regulate: "public health, safety environment or public morals, social or consumer protection or promotion and protection of cultural diversity". The text further provides that the discontinued granting of subsidies, including State aid, cannot be viewed as an expropriation.

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<sup>2</sup> Proposal for services, investment and e-commerce text tabled for discussion with the US in the negotiating round of 12-17 July 2015, [http://trade.ec.europa.eu/doclib/docs/2015/july/tradoc\\_153669.pdf](http://trade.ec.europa.eu/doclib/docs/2015/july/tradoc_153669.pdf), page 5



### TABC position

The European Union and United States agreed that a primary objective of TTIP is to establish high standards for future investment treaties. To be effective in providing meaningful investment protections, it is critical that the agreement includes strong substantive investment protections.

Substantive protection of investments is not at odds with the right to regulate in the public interest. Existing investment agreements have been applied consistent with the right to regulate. For example, tribunals have thrown out claims that inappropriately challenge legitimate regulations and have forced investors to pay the costs of the arbitration when bringing frivolous claims.

The Commission's draft sets forth excessively broad language on the right to regulate, including general exceptions, such as "social protection", "public morals" and "protection of cultural diversity."<sup>3</sup> This proposed text does not clarify how to distinguish between the State's right to regulate, on one hand, and thinly veiled protectionist measures used to harm investors on the other hand.

TABC observes that States win ISDS cases about twice as often as investors. It is thus particularly important that particularized concerns about State regulation should be addressed through clear definitions of key substantive protections rather than through a list of general exceptions. While it is important to ensure that States have the freedom to enact reasonable, non-discriminatory regulations, substantive investment protections must ensure that States do not enact unreasonable, discriminatory, or unduly harmful regulations.

### ***Fair and Equitable Treatment (Section 2, Article 3)***

#### Summary

The draft text narrowly defines "fair and equitable treatment" (FET) and "full protection and security". The text details a closed list of what constitutes a breach of the obligation of FET.

#### TABC position

FET ensures foreign investors receive a minimum level of protection against harmful government actions against their investments. The United States has traditionally tied this protection to the minimum standard under Customary International Law.

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<sup>3</sup> Draft Investment Text, Article 3, para 5,  
[http://trade.ec.europa.eu/doclib/docs/2015/september/tradoc\\_153807.pdf](http://trade.ec.europa.eu/doclib/docs/2015/september/tradoc_153807.pdf)



As the Commission itself has recognized, a FET provision is incorporated in almost all modern investment agreements, including those of EU Member States and the United States. Since it is not practical to anticipate the range of future State actions taken against investors, the FET standard should remain sufficiently flexible to allow future, unanticipated investor mistreatment to be addressed.

TABC supports the inclusion of an “umbrella clause” described in Article 3. Such a clause guarantees that if a host State fails to abide by its contractual obligations to investors, they may have recourse under the ISDS provisions of the agreement. An umbrella clause, viewed together with the agreement’s other substantive investment protections, provides greater certainty to foreign investors who are often making complex foreign investments that include contractual and other undertakings.

TABC welcomes the Commission’s aim to provide legal certainty and clarity on the scope of application of the FET clause. At the same time, TABC does not endorse the inclusion of a closed, exclusive list of State measures and actions. For instance, it is problematic that “full protection and security”<sup>4</sup> is limited to physical assets.

Overly narrow definitions limit the key strength of the FET standard, particularly as the American and European economies progress and grow throughout the term of an agreement. It is important for an investment agreement to respond to arbitrary and discriminatory action across a range of factual circumstances. The Commission’s proposals in the draft text to perpetuate narrow definitions risk weakening investment protection further. This is a worrying trend and out of line with the goal of establishing a gold standard agreement. TTIP should strive to be a positive model for a new generation of investment agreements with highest standards of protection rather than an agreement that increases uncertainty for investors.

Further, terms such as “manifest arbitrariness” and “fundamental breach”<sup>5</sup> create an unclear, very narrow standard. Such an approach runs the risk of unduly restricting investor protections. This terminology is open to interpretation, therefore increasing ambiguity by introducing a point of distinction with prior awards.

## ***Expropriation (Section 2, Article 5 and Annex I)***

### *Summary*

The draft text narrowly defines direct and indirect expropriation. The investor is granted the right to have its claim reviewed by a judicial or other independent authority of the State. The proposal also states that a determination that a measure is inconsistent with

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<sup>4</sup> Draft Investment Text, Article 3, para 2

<sup>5</sup> Ibid



the WTO's Trade-Related Aspects of Intellectual Property Rights (TRIPS) "does not establish that there has been an expropriation". Moreover, inconsistency with TRIPS or Chapter X (Intellectual Property) of TTIP would not suffice to establish that there has been an expropriation".

#### TABC position

TABC supports strong protections in a TTIP investment chapter against all forms of expropriation, including both direct and indirect expropriation. The legal standard for this protection is well-established in investment treaties and is part of customary international law: foreign investments shall not be expropriated except for a public purpose, on a non-arbitrary or discriminatory basis, with full due process, and with prompt, adequate and effective compensation.

It is important that a TTIP investment chapter apply the same standard of protection for indirect expropriation as it does for direct expropriation. The TTIP's protection against indirect expropriation should encompass any covered investment, including intellectual property rights, without qualification. We find the language about TRIPS quoted above to be unnecessary and ambiguous. A claim of expropriation of IP rights should not be treated any differently than a claim of expropriation of tangible property.

On the other hand, TABC fully recognizes that reasonable State measures or actions that regulate investment might not necessarily constitute an expropriation: a fact-specific inquiry is required for each instance.

The language proposed in the text, alongside the proposal's FET standards, sets forth an unreasonably high threshold for violation of the expropriation standard in which the "impact of a measure or series of measures is so severe in light of its purpose that it appears manifestly excessive."<sup>6</sup> This threshold is too narrow and could be problematic for investors bringing claims on the basis of indirect expropriation, thus rendering the last resort to fair resolution of disputes under a minimum standard of the rule of law rather irrelevant in practical terms.

### **Investment Court System**

#### ***Tribunal of First Instance and Appeal Tribunal (Section 3, Sub-Section 4)***

##### Summary

The draft text significantly revises the method for the settlement of investment disputes, as compared to provisions outlined in the EU's recently concluded trade agreements

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<sup>6</sup> Draft Investment Text, Annex I, para 3



with Canada and Singapore. The text proposes the creation of a Tribunal of First Instance (“Investment Tribunal”) and an Appeal Tribunal.

The Commission proposes to have Judges for the Investment Tribunal chosen from a pre-established list. The European Union and United States would appoint 15 judges to the Tribunal: five from European Union Member States, five from the United States and five from third countries. These Judges would “desirably” have expertise in international investment law, trade law and the resolution of disputes.

Three of the appointed Judges would preside over a Tribunal: one from the European Union, one from the United States, and one from the third country. The Judge from the third country will serve as Tribunal chair.

The text further proposes a permanent Appeal Tribunal with six Members: two from the European Union, two from the United States, and two from third countries.

Judges and Tribunal Members would be appointed for a six-year term, with one possible renewal. Judges and Tribunal Members would be paid a monthly retainer fee that could be transformed into a regular salary, subject to working for the Tribunal full-time and not otherwise employed.

The text outlines specific qualifications to serve as a Judges of the Tribunal and Members of the Appeal Tribunal, such as prohibition from serving as legal counsel in any investment disputes.

#### TABC position

The proposed investment court system is not an impartial, neutral forum for investors and States to resolve disputes. Arbitrators in the proposed court will be selected by the governments, but it is not clear how they will be selected. The court will not be effective if the selection process lacks impartiality and transparency.

Neither the claimant nor the State have the right to select a Judge or Member of the Appeal Tribunal as each will be selected at random from a predetermined list. The choice of the arbitrator is a vitally important element for both the claimant and the respondent State, and the parties should not be limited to a predetermined list. The creation of an approved list of arbitrators has proven problematic in practice. ICSID, for example, has difficulty keeping its roster of arbitrators up to date, and since no one can anticipate which disputes may arise, the arbitrators are chosen in a relative vacuum.<sup>7</sup>

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<sup>7</sup> Under the currently used International Centre for Settlement of Investment Disputes (ICSID) system, each party selects an arbitrator and the third is chosen jointly or appointed by the ICSID Secretary General. These arbitrators are usually selected from the ICSID roster, which is created has a list of over 900 arbitrators all nominated from the 151 contracting parties. Further, the arbitrators cannot be the same nationality of the parties in dispute.



The limited list and random assignment could result in a panel in which the Judges and Members lack the case-specific knowledge in dealing with highly technical claims and industries often sought by using traditional ISDS. The ethical requirements limit a Judge or Member from acting as legal counsel in any investment disputes, which could further limit their technical expertise.

The Tribunal may further result in extra costs and time delays. The small roster of arbitrators could prove problematic to the extent that if potential conflicts are a concern and there is an interest in seeing a diverse pool of arbitrators in ISDS disputes, a closed list can unfortunately limit the options available to parties. This is especially true if certain cases require an in-depth technical expertise and background of the arbitrator.

Furthermore, the Commission still needs to address significant questions about how the Tribunal will operate. The Tribunal has the authority on creating its rules of procedure according to the draft text. It is uncertain, therefore, how the Tribunal will coexist with existing and future international investment rules created by ICSID or other investment arbitration systems.

It is also not clear where the Tribunal will be physically located. The draft text provides the potential of the Tribunal to evolve into a Permanent Court of Arbitration but makes no mention of where Judges and Members will meet to hear cases.

TABC agrees that the TTIP can be a vehicle for the European Union and the United States to assess together the potential for an appellate mechanism to review Investor-State Dispute Settlement (ISDS) decisions. In principle, such a mechanism would provide for more consistency, coherence in the system, and certainty for investors. Still, modeling a mechanism on the WTO Appellate Body which is designed on a “state-to-state dispute settlement” must take into account that investment cases under TTIP would deal with “investor-to-state dispute settlement”.

The Appeal Tribunal will mean extra costs and time delays for the parties seeking resolution. This may not end up being favorable for either party to the dispute, including for respondent States, given that in the current ISDS system States win cases the vast majority of the time.

### **Additional Comments**

- TABC supports a definition of “investor” that makes clear that the pre-establishment phase of an investment is covered and can be enforced through dispute settlement. This is particularly critical in setting a global standard that will help protect EU and US investors seeking to enter other markets on fair and non-discriminatory terms. Investors do not have the right of establishment in the Commission’s text. Still, by limiting the definition of an investor to “for-profit”



- investors leaves certain types of actors such as non-profit NGOs outside the protection scope.
- Article 14 requires investors to withdraw from domestic proceedings before submitting a claim to ISDS (“no u-turn” approach) to avoid parallel claims. The objective to limit parallel awards is useful.
- TABC supports transparency in the dispute settlement process using the United Nations Commission on International Trade Law (UNCITRAL) rules on transparency as described in Article 18. While the improvements are significantly greater than existing European Union Member State investment treaties, TABC notes that these clauses have been in existence in the US investment agreements as well as in recent updates of the ICSID and UNCITRAL rules. Yet, commercially sensitive or confidential information must be exempt from being publically shared in documents or with experts or third parties. Similar, personal rights of people involved in cases must be observed.
- TABC opposes the “loser pays” rule established in Article 28 but notes the Tribunal may decide not to implement this principle. Many cases are difficult and complex, and losing a case does not necessarily mean that the loser should bear all costs. We believe the better practice is to provide the tribunal with discretion to determine fees and costs. If inclusion of this principle is to address frivolous claims, TABC notes that such provisions are already included in Articles 16 and 17.
- The enforcement provisions under Article 30 make no mention of how awards tie into the enforcement mechanisms in the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, which is included in CETA. Instead, States will recognize awards as if they are a “final judgement” in a domestic court and execute the award according to laws with that State. Enforcement problems already exist in the current system so it is vital that investors can count on the dispute settlement system. This would create further problems if the Tribunal is to be multilateralized.