

**DIRECTORATE-GENERAL FOR EXTERNAL POLICIES**  
**POLICY DEPARTMENT**



**INVESTOR-STATE  
DISPUTE SETTLEMENT  
(ISDS) PROVISIONS IN  
THE EU'S INTER-  
NATIONAL INVEST-  
MENT AGREEMENTS**

**VOLUME 1-WORKSHOP**

**INTA**





DIRECTORATE-GENERAL FOR EXTERNAL POLICIES OF THE UNION

**DIRECTORATE B**

POLICY DEPARTMENT

**WORKSHOP**

**INVESTOR-STATE DISPUTE SETTLEMENT (ISDS)  
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AGREEMENTS**

**VOLUME 1 -WORKSHOP**

# WORKSHOP

POLICY DEPARTMENT, DG EXPO  
FOR THE COMMITTEE ON INTERNATIONAL TRADE (INTA)

01.04.2014

PAUL HENRY SPAAK BUILDING

9.00-11.00 ROOM: PHS 1A002

## INVESTOR-STATE DISPUTE SETTLEMENT PROVISIONS IN THE EU'S INTERNATIONAL INVESTMENT AGREEMENTS



CHAIRMAN: VITAL MOREIRA

Contacts and registration: [poldep-expo@ep.europa.eu](mailto:poldep-expo@ep.europa.eu)

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- Volume 2: Studies

### **AUTHORS:**

Dr Pieter Jan KUIJPER, Professor, University of Amsterdam, The Netherlands  
Dr h.c. Ingolf PERNICE, Professor, Humboldt-Universität zu Berlin, Germany  
Dr Steffen HINDELANG, LL.M., Associate Professor, Freie Universität Berlin, Germany  
Ms Meg KINNEAR, Secretary-General, ICSID, USA  
Michael SCHWARZ, Research Assistant, Humboldt-Universität zu Berlin, Germany  
Martin REULING, Research Assistant, University of Amsterdam, The Netherlands

### **ADMINISTRATOR RESPONSIBLE:**

Elfriede BIERBRAUER, Roberto BENDINI  
Directorate-General for External Policies of the Union  
Policy Department  
SQM 03Y53  
rue Wiertz 60  
B-1047 Brussels

Editorial Assistant: Györgyi MÁCSAI

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## PROGRAMME OF THE WORKSHOP

### DIRECTORATE GENERAL FOR EXTERNAL POLICIES

Policy Department and Committee on International Trade



## WORKSHOP

### Investor-State Dispute Settlement (ISDS) provisions in the EU's International Investment Agreements

Brussels  
Paul Henri Spaak Building  
**Room PHS 1A002**  
**Tuesday, 01 April 2014**  
(09:00-11:00 h)

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## PROGRAMME

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|-------|--|
| 09.00 | <b>Welcome and introduction to the workshop by<br/>INTA Chairman <b>Professor Vital MOREIRA</b></b>  |
| 09.15 | <b>Panel:</b><br><b>European Commission's strategy in the field of international investment<br/>protection</b><br><b>Mr. Rupert SCHLEGELMILCH</b> , Director, European Commission, DG Trade          |
| 09.25 | <b>Investment protection agreements as instruments of international economic<br/>law</b><br><b>Professor Pieter Jan KUIJPER</b> , University of Amsterdam  |
| 09.35 | <b>Investor-State Dispute Settlement (ISDS) and alternatives of dispute resolution<br/>in international investment law</b><br><b>Professor Steffen HINDELANG</b> , Freie Universität, Berlin         |
| 09.45 | <b>European Union law and investment protection agreements</b><br><b>Professor Ingolf PERNICE</b> , Humboldt-Universität zu Berlin   |
| 09.55 | <b>Dispute Settlement Resolution in practice</b><br><b>Ms Meg KINNEAR</b> , Secretary-General of ICSID (International Centre for Settlement of<br>Investment Disputes), World Bank Group, Washington |
| 10.05 | <b>Q&amp;A session</b>   |
| 10.55 | Closure of the workshop by INTA Chairman <b>Prof. Vital MOREIRA</b>  |

## **BIOGRAPHICAL SUMMARIES OF THE SPEAKERS**

### **DIRECTORATE GENERAL FOR EXTERNAL POLICIES**

Policy Department and Committee on International Trade



### **WORKSHOP**

#### **Investor-State Dispute Settlement (ISDS) provisions in the EU's International**

#### **Investment Agreements**

Brussels  
Paul Henri Spaak Building  
**Room PHS 1A002**  
**Tuesday, 01 April 2014**  
(09:00-11:00 h)

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### **BIOGRAPHIES**

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#### **Prof. Pieter Jan KUIJPER**

Pieter Jan Kuijper returned to the University of Amsterdam as Professor in the Law of International (Economic) Organizations in 2007. Before that he finished a long career in international organizations, mainly spent in the Legal Service of the European Commission, first as Director of the Legal Affairs Division of the WTO Secretariat (1999-2002) and next as Director of the Division for External Relations and International Trade in the Legal Service of the European Commission (2002-2007). His main research interests are: the comparative approach to international organizations; EU institutional law, in particular foreign relations law (including trade policy); WTO law; relations between EU law, WTO law and general international law. He is the author of some 90 articles in these different fields of international and European law. He may be contacted at [P.J.Kuijper@uva.nl](mailto:P.J.Kuijper@uva.nl).

#### **Prof. Steffen HINDELANG**

Steffen Hindelang is Associate Professor at the Department of Law of Freie Universität Berlin where he teaches international economic law, esp. international investment law, EU law and German public law. Previously he was Senior Research Associate and Lecturer at Humboldt-Universität zu Berlin, Germany, School of Law (2010-11). He is also a Senior Fellow of the Walter Hallstein Institute of European Constitutional Law Berlin and an academic advisor to the International Investment Law Centre Cologne (IILCC). He was guest professor at Bocconi University Milan, the University of Lausanne, and the Charles University Prague. His research interests comprise international economic law, esp. international investment law, international arbitration and dispute settlement, EU law, and German constitutional and administrative law. He advised, inter alia, governments in international investment disputes and on matters of reform of the current international investment law regime. He may be contacted at [mail@steffenhindelang.de](mailto:mail@steffenhindelang.de).



## **Prof. Ingolf PERNICE**

Professor Ingolf Pernice is the director of the Walter Hallstein-Institute for European Constitutional Law at Humboldt University Berlin. He studied in Marburg, Geneva, Freiburg and at the College of Europe in Bruges. After his legal clerkship at the Higher Regional Court in Munich and his doctorate on European Fundamental Rights, he became an official of the European Commission in Brussels in 1980, first in DG Competition, later in the Legal Service. In 1987 he did his state doctorate about 'equity and hardship clauses in public law' in Bayreuth. In 1993 he joined the Johann Wolfgang Goethe-Universität Frankfurt as professor of public law, public international law and European law. Since 1996 he teaches at the Humboldt-Universität zu Berlin. From 1997 to 2001 he was a member of the 'European Forum for Environment and Sustainable Development' of the European Commission. In 1997, he founded the Walter Hallstein-Institute for European Constitutional Law and in 1998 the European Constitutional Law Network. He is the host of the lecture series 'Forum Constitutionis Europae' (FCE) and 'Humboldt-Reden zu Europa' (HRE). Since 2006 he is leading the DFG – Graduate School, Multilevel Constitutionalism. European Experiences and Global Perspectives" and from 2006 to 2008 he was the dean of his faculty. After his visit as a senior research fellow at the Law and Public Affairs (LAPA)-Programme and guest professor in Princeton University in 2008/09, he expanded his research from European commercial law, environmental law, law of the European Monetary Union and constitutional law to issues of global constitutionalism. Since 2011 he is Co-Founder and Director of the Humboldt Institute for Internet and Society (HIIG). He may be contacted at [ip@whi.eu](mailto:ip@whi.eu).

## **Ms Meg KINNEAR**

Meg Kinnear is currently the Secretary-General of the International Centre for Settlement of Investment Disputes (ICSID) at the World Bank. She was formerly the Senior General Counsel and Director General of the Trade Law Bureau of Canada, where she was responsible for the conduct of all international investment and trade litigation involving Canada, and participated in the negotiation of bilateral investment agreements. In November 2002, Ms Kinnear was also named Chair of the Negotiating Group on Dispute Settlement for the Free Trade of the Americas Agreement.

From October 1996 to April 1999, Ms Kinnear was Executive Assistant to the Deputy Minister of Justice of Canada. Prior to this, Ms Kinnear was Counsel at the Civil Litigation Section of the Canadian Department of Justice (from June 1984 to October 1996) where she appeared before federal and provincial courts as well as domestic arbitration panels.

Ms Kinnear was called to the Bar of Ontario in 1984 and the Bar of the District of Columbia in 1982. She received a Bachelor of Arts (B.A.) from Queen's University in 1978; a Bachelor of Laws (LL.B.) from McGill University in 1981; and a Master of Laws (LL.M.) from the University of Virginia in 1982.

Ms Kinnear has published numerous articles on international investment law and procedure and is a frequent speaker on these topics. She is a co-author of *Investment Disputes under NAFTA* (published in 2006 and updated in 2008 & 2009). She also co-authored texts on Canadian legal procedure including *Federal Court Practice* (1988-1990, 1991-1992, and 1993-2009 annually) and *1995 Crown Liability and Proceedings Act Annotated* (1994).

## PART I: STATEMENT FROM THE EC - THE EUROPEAN COMMISSION'S STRATEGY IN THE FIELD OF INTERNATIONAL INVESTMENT PROTECTION

*by Rupert Schlegelmilch*

### 1. OPENING REMARKS

- The EU is collectively the **biggest investor in the world**. Only in FDI, we have a stock of investment abroad of more than 7 trillion euros.
- We have inherited a well **consolidated practice of Member States**, who have been **the leaders of investment agreements** for more than 50 years. About half of the existing investment agreements are agreements between individual Member States and third countries.
- This inheritance came with **challenges and responsibilities**, the most important of which is that we must prove that all of us at the EU level can do better.
- We have been hearing the **criticisms** to the investment arbitration system. The absence of a model treaty has allowed us to use the constructive aspects of these criticisms in order to **reset our policy-making compass to point towards more balance** between investment protection and the capacity of states to regulate in the public interest.
- The need to achieve this balance and to improve the system goes hand in hand with action: **Doing nothing is not an option for many reasons:**
  - (i) If we do nothing, **the current arrangements** –those which receive the strongest criticism- **will stay in place** and the potential for future abuse will continue: standards of treatment will remain vague and ISDS will not be as transparent.
  - (ii) **The EU is a major player** in the global scene: we cannot hide behind our finger by not taking a stance on a debate which is likely to change investment protection rules worldwide.
  - (iii) There is a pragmatic need to **protect EU investments** abroad.
  - (iv) There is an imperative drive to do so **without undermining the capacity of States to regulate**.
- I will briefly take you through the steps that the EU has already taken to improve the investment regime through its negotiations with Canada and Singapore. But before doing so it is crucial to underline two points:
  - (i) Building a strategy for EU investment is a process: Last week Commissioner De Gucht launched a public consultation for the investment protection and the ISDS approach in the TTIP. The Commission will look carefully into the replies to be received and will cater them in its policy reflections for the handling of the TTIP negotiations. We don't rule out that we would also see what the lessons to be learnt for other future negotiations are.
  - (ii) It is not only for EU agreements that the Commission is pushing for improvements. At international level, the European Commission has in the last 3 years been instrumental in getting new UN rules on transparency in ISDS disputes off the ground. These new rules on transparency - that entered into force the 1st of April - will allow the public access to hearings in ISDS disputes and will make submissions and awards publicly available. To further support the push for transparency, the **Commission plans to provide a contribution of € 100.000 to set up a publicly accessible data base (repository) on ISDS cases**.

## 2. WHAT ARE THE IMPROVEMENTS INTRODUCED BY THE EU'S INVESTMENT POLICY?

### 2.1 Part 1: Investment protection standards

#### 2.1.1 Right to regulate

- **The right to regulate is affirmed as a standing principle.** This means that, when interpreting the content of the agreement, arbitral tribunals must take into account this principle, i.e. that the intention of the Parties when concluding the agreement was not to undermine in any way the right to regulate.
- **EU Agreements firmly state that measures taken for legitimate public purposes, such as health or environment protection, cannot be considered equivalent to an expropriation (indirect expropriation),** unless they are manifestly excessive in light of their purpose.

#### 2.1.2 Fair and equitable treatment

Clear listing of the **elements of the obligation to provide fair and equitable treatment (FET)**. In order to establish a breach of FET, **the investor would have to prove that the measure constituted a breach of fundamental rights** such as a breach of due process, targeted discrimination, manifest arbitrariness, duress, coercion or harassment. EU agreements also make it clear that the legitimate expectations of the investor do not imply the **right to be protected from changes in the general legislation** of the host State, such as for instance a change in the minimum wage or a ban on fracking.

#### 2.1.3 Full protection and security

The obligation to provide "**full protection and security**" is clearly limited to the duty to ensure physical protection. It **cannot be interpreted as covering legal security and as requiring a State not to change its legislation.**

#### 2.1.4 Prudential measures

It is clarified that Parties to an agreement are entitled to take measures for prudential reasons, including measures to ensure the integrity and stability of their financial system. In addition, EU agreements contain specific **exceptions** applying in situations of crisis, such as in circumstances of difficulty for the exchange rate policy or monetary policy, balance of payments or external financial difficulties, or threat thereof.

#### 2.1.5 "Shopping" favourable provisions from other agreements

EU agreements clarify through specific provisions that the MFN clause cannot be interpreted so as to allow "importation" of either substantive (e.g. expropriation) or procedural (e.g. ISDS provisions) clauses contained in other agreements.

### 2.2 Part 2: ISDS system

On ISDS, our objective is to have a state of the art ISDS system for all EU trade and investment agreements.

Main innovations in the EU's approach to ISDS:

- **Preventing abuse of the ISDS system: Parallel claims will not be allowed** under EU agreements. ISDS Tribunals will be able to quickly and easily dismiss **unfounded and frivolous claims**. The **losing party will bear the costs of the arbitration** also those of the responding state.

- **Narrowing the scope of ISDS to prevent claims by "shell companies" and "Treaty shopping".** Investors must have substantial business activities in the territory of the host country in order to claim protection.
- **Appointment and ethical conduct of arbitrators:** All arbitrators must abide by a code of conduct with specific and binding obligations for arbitrators, including on conflicts of interests and ethics together with rules on how these should be enforced. Also under EU agreements, in case of disagreement on the chair of the tribunal, the arbitrator will be chosen from a pre-agreed list of 15 arbitrators. This will allow states to maintain certain amount of control over the tribunal's composition.
- **Clarifying and limiting the powers of tribunals:** EU agreements will make clear that ISDS tribunals cannot overturn measures, and that compensation cannot be higher than the financial loss.
- **Transparency:** under EU agreements it will be mandatory on the disputing parties to make all submissions and awards available to the public. At present the disputing parties must both agree to release documents to the public.
- Possibility to **appeal** ISDS rulings

## **PART II: OUTLINES BY THE EXPERTS**

### **1. INVESTMENT PROTECTION AGREEMENTS AS INSTRUMENTS OF INTERNATIONAL ECONOMIC LAW**

*by Dr Pieter Jan Kuijper*

#### **1.1 History and Background of Bilateral Investment Treaties (BITs) and the international investment dispute settlement infrastructure**

Motives and Objectives behind BITs

The first treaty of this kind established between the Federal Republic of Germany and Pakistan in 1959 was made to enable the state of Germany to insure or give guarantees to outward investment in countries with which it had concluded such an agreement (a self-imposed legal requirement).

Behind this lies the old 19<sup>th</sup> century dispute between European countries and the US on one side and the Central and South-American countries on what constitutes the proper treatment of foreign investment: national treatment or a minimum standard of treatment independent of the former. BITs provide a solution to this dispute by laying down a combination of elements from both positions (in varying mixtures).

There are/were also somewhat idealistic motives: increase the attractiveness of developing countries with weak institutions (in particular the judicial power) for foreign investment from the developed world, since official development aid could no longer provide the amount of investment developing countries needed.

It was this approach that led to the creation (by the World Bank) and growing relevance of the International Center for Settlement of Investment Disputes (ICSID) as part of international investment dispute settlement. Initially this Center languished somewhat, but as from the late '80's under a renewed impulsion of the Bank, ICSID became a centre of expertise on investment dispute settlement and contributed considerably to the construction of contemporary investment dispute settlement. In the wake of ICSID other dispute settlement centers came up: PCA, Paris ICC, London, Stockholm.

On the side of the developing countries another motive apart from attracting foreign investment has come up: their willingness to conclude BITs has become part of the elements that rating agencies employ in determining the credit rating of a country. This may explain that some countries that do not have a happy experience with BITs, are willing to maintain them.

Looking at the preambles of modern model BITs, one comes to the conclusion that the development motives have been exchanged largely for purely utilitarian reasons to conclude BITs. Facilitating the mutual flow of capital and its most efficient use are prominent in such clauses. There are only a few countries that still openly refer to development motives. This is a reflection of the fact that BITs are concluded more and more between countries with a similar level of development or only limited differences in development: cf. the case of Turkey. CETA and TTIP are also examples.

## 1.2 Usual elements of contemporary investment treaties (based on treaty practice)

- a. Investment clauses (access and facilitation) and investment protection clauses: they are conceptually different, but they are integral as a package.
- b. Core elements of investment treaties
  - i. Definitions
    1. Technically very important, but not discussed today. What is an investment? Who is an "investor of the other party"? Etc.
  - ii. Investment Clauses: access and non-discrimination
    1. National Treatment (NT).  
Foreign investors have to be treated as national investors.
    2. Most-Favoured Nation Clauses (MFN)  
All foreign investors have to be treated in an equal manner.
    3. Minimum standard of treatment / Fair and equitable treatment (FET).  
Foreign investors are treated to a standard that is considered acceptable between the parties and normally higher than NT.
  - iii. Investment Protection Clauses
    1. Free Transfer of Funds  
Import and export of capital, dividends, profits and eventual compensation for expropriation is free.
    2. Nationalization protection and compensation clauses  
Direct and indirect nationalization  
Prompt, adequate and effective compensation for the full value of the investment in case of expropriation in the public interest is guaranteed.
    3. Full protection and security.  
Are the investments adequately protected by the authorities of the host country in cases of social unrest (strikes) and civil disturbances or even civil war?
  - iv. Dispute Settlement Clauses
    1. Consultations:  
Obligatory stage of amicable settlement in most BITs.
    2. International Arbitration:  
Exhaustion of local remedies, competent bodies, applicable rules, jurisdiction.
    3. Conflicts of Jurisdiction

## 1.3 Relation between international investment treaties and international trade law

- a. How international investment became interrelated with international trade law and policy
  - i. The national treatment clause of GATT was so broad that it could include certain trade-related investment measures. This came to the fore in an old GATT dispute settlement case: *Canada – Foreign Investment Review Act*, which declared so-called performance requirements imposed on foreign investment in goods manufacturing illegal. The result of this case was codified in the *Agreement on Trade Related Investment Measures*, which became part of the WTO. There is a clear overlap here between WTO and BITs, especially in the field of NT.
  - ii. Inclusion of trade in services (especially in Mode 3, commercial presence) in the drafting of the GATS. This led to most favoured nation and national treatment clauses being made

applicable to this way of providing services across frontiers (at least if services commitments were made by Members) This basically covers the access and treatment of foreign investment in the services sector, which is normally also covered by BITs.

- iii. Treatment of IP rights in BITs as investments entails the consequence that these are covered twice by MFN and NT and dispute settlement clauses under both WTO TRIPs Agreement and BITs.

- b. International trade law and investment law: Overlapping areas and possible conflicts.

The above demonstrates how international trade law and international investment law are closely interrelated. It is natural that they should be part of the same “package” of negotiations. Both overlap between trade law and BITs and its absence may cause problems. Overlap may cause problems because of incompatibilities, especially because of differences in scope as a consequence of differences in exceptions clauses. Real conflicts are less likely, also because the notion of conflict is normally interpreted restrictively. Note the differences between the two approaches where procedures of dispute settlement and its remedies are concerned. State to State and Individual to State procedures; emphasis on withdrawal of the measures (WTO) and on the payment of damages (BITs).

- c. Investment treaty negotiations as part of EU competences.

In the light of the two preceding sections, it is obvious how foreign direct investment both in services and in the production of goods was destined to become a part of the common commercial policy powers of the European Union. The close link between access for investment and investment protection as well as litigation on both subjects pleads for an integrated approach by the Union and on behalf of the Union by the Commission, the institution that has considerable expertise and experience in both domains. However, the legal controversies over exclusive or mixed competences in this domain will not be discussed.

## **1.4 Conclusions**

Main points from the three preceding sections.

## 2. INVESTOR-STATE DISPUTE SETTLEMENT (ISDS) AND ALTERNATIVES OF DISPUTE RESOLUTION IN INTERNATIONAL INVESTMENT LAW

by Dr Steffen Hindelang

Mr. Chairman, Ladies and Gentlemen,

At the outset, allow me to thank you, Mr. Chairman, and the European Parliament for the opportunity to contribute to this workshop with some initial observations on “investor-state dispute settlement (ISDS)” to facilitate the following discussion.

Since the 1970s, almost any bilateral and regional investment instrument has provided for investor-state dispute settlement. On the basis of these agreements a foreign investor can commence international arbitration against its host state claiming administrative, regulatory, or judicial measures are in violation with investment protection standards.

At a global level rising numbers of investor-state disputes and newly signed investment agreements suggest the *continuous importance and* attractiveness of this dispute settlement mechanism. Yet, we also see *contestations*. A few countries did not renew or even terminated existing investment instruments while others have withdrawn from the ICSID-Convention.

What does this mean for the European Union? Simply carrying on appears no sustainable option anymore. Modern investor-state dispute settlement practice faces massive public criticism: non-transparent proceedings, hardly predictable outcomes, inappropriate interferences with democratic policy choices in host states, and considerable financial risks, just to mention a few controversial points.

What has been voiced and critically discussed in parts of academia and expert circles for some time has now turned into a noisy global debate, which also has to be addressed by the European Union. Popular opposition by civil society campaigners has helped turn the spotlight on serious deficits of investor-state dispute settlement. However, we must not throw out the champagne with the cork.

The EU in general and this Parliament in particular have the chance to provide significant impetus for correcting mistakes of the past and preserving the virtues of this dispute settlement mechanism for the future.

Speaking of virtues: investor-state dispute settlement is perceived as a forceful tool to *manage political risk* and to *promote an international rule of law*. It is said to *make substantive commitments in investment instruments credible* and, at the same time, contributes towards a *de-politicisation of individual investment disputes*.

Investor-state dispute settlement's contribution to the promotion of an international rule of law should be stressed in particular. Bilateral and regional investment protection treaties are the extension of the century-old idea within public international law that everyone is entitled to a minimum standard of treatment abroad at any given time. Investor-state dispute settlement is the key mechanism to hold the host state accountable for conduct falling short of certain standards without having (exclusively) to rely on domestic judicial relief, which might be unavailable just in the moment when it is desperately needed.

Certainly, it is true – and regrettable at the same time – that not all elements of an international minimum standard for the treatment of aliens were developed further with equal focus and lasting success. The *grand idea* underlying these efforts should, however, not be forgotten: limiting



governmental arbitrariness by stipulating *legal* standards to the benefit of foreign individuals and corporations enforceable in impartial arbitral proceedings.

It might, therefore, be almost tragic to see some of those civil society groups that have vigorously fought for human rights and an international rule of law now find themselves on the side of those states that blatantly call for weakening exactly this international rule of law.

Just to be clear on this point: investor-state dispute settlement as it currently operates is far from perfect. However, demanding to significantly weaken or even to completely renounce investor-state dispute settlement would call into question part of the achievements made with regard to an international rule of law. At the same time it is also clear that aberrations of investor-state dispute settlement practice must be cut back to the concept's initial idea: providing a *safety net* in case the *primary means of redress available in a host state* fail to prevent or remedy abuse of sovereign power. Put differently, international investment law and investor-state dispute settlement can only regain legitimacy if the latter does *not aim at replacing or turning into an alternative to domestic administrative and judicial safeguards*, but instead backs them up in case of failure.

The idea of providing a fallback, a last line of defence, can equally be applied to developing as well as developed legal systems if we accept that even the most advanced legal system may fall short of certain standards in exceptional cases. In principle, providing for investor-state dispute settlement also among developed countries signals that international investment law is not about "neo-colonialism" or directed against developing countries, but rather about an international rule of law.

However, if not carefully designed, allowing for investor-state arbitration may come with significant political, legal, and economic costs, as its current practice demonstrates. Out of several serious concerns with regard to investor state dispute settlement, one appears particularly troubling. Current investor-state dispute settlement practice is perceived as not paying sufficient attention to legitimate public interests such as human rights, environmental protection, or public health. It is said to excessively curtail national regulatory space to implement policies directed at general welfare.

Investment tribunals have been dealing with *highly sensitive political issues*. They have been asked to rule on cigarette plain packaging in Australia and Uruguay, the nuclear power phase-out in Germany, or crisis-related financial austerity measures taken by Belgium in the course of the European financial crisis. In the past, tribunals have repeatedly faced questions of whether they are willing and able to sufficiently take into account public interests. In legal terms, what has been criticised is that decisions of tribunals seem to *not* accurately reflect the "right balance" which the state parties to the investment instrument meant to strike between private property protection and public interests in their investment treaties.

*Securing the "right balance"* between private and public interests will also be central for the European Union in its unfolding international investment policy. Striking the "right balance" does not only mean securing an acceptable outcome in treaty negotiations with other states. The EU must also ensure that the *balance struck will not subsequently be distorted in dispute settlement*.

Regardless of the controversy of whether there might be incentives in the structure of investor-state dispute settlement which work in favour of private interests, or whether a re-balancing in favour of private interest is simply the consequence of some arbitrators "merely" wanting to strike some sort of equitable compromise in the particular case, state parties are constantly threatened with losing power over the ultimate determination of the content of their investment instrument.

One phenomenon observed in current investor-state arbitration practice seems to be particularly risky in this respect: the so-called system of "de facto precedent". A significant number of investment tribunals tend to justify their interpretation of a treaty provision exclusively or largely by referring to the

interpretation of similar-worded provisions adopted in previous awards rendered on the basis of different investment instruments. What these tribunals basically engage in is “cherry-picking” previous awards allegedly supporting a tribunal’s reading of a certain treaty provision. In doing so, they sidestep the binding methodology of interpreting international treaties found in the Vienna Convention on the Law of Treaties. These “Vienna rules” are, however, not merely a technicality. They secure a transparent interpretative process and a legitimate result most close to *the intention of the state parties to the treaty*.

Arbitrarily choosing from a selection of interpretations of similarly worded provisions previously developed in different, usually incomparable, bilateral contexts carries the risk that the state parties’ intentions with regard to the substantive standards in a specific investment instrument might be replaced by other, extrinsic intentions. It lurks exactly here: the threat that tribunals would free themselves from the bonds of their masters, the state parties to the investment treaty.

An effective instrument which lends itself to preventing such distortions of the “right balance” between public and private interests is the power of authoritative interpretation of an investment instrument vested by the state parties. Authoritative interpretation here means nothing other than that the state parties have the “last word” on the meaning given to the provisions of a treaty. However, they have yet to make use of these powers more proactively.

NAFTA experience is telling that a treaty committee staffed with representatives from the respective state parties and charged with the power to authoritatively interpret the substantive standards contained in the treaty can help hedge in (to some extent) power-seizure processes inherent to treaty interpretation by ad-hoc tribunals in the course of dispute resolution. At least in this respect it is to be welcomed that the EU seems to be following the NAFTA path when negotiating with Canada and the USA.

If one wishes to tie tribunals even closer to the intentions of the state parties an investment instrument could provide for a mandatory review process of draft awards by the state parties or a treaty committee. If the state parties conclude that the interpretation of the investment instrument does not mirror their mutual intentions they could refer the draft award, along with interpretative guidance, back to the tribunal.

The activation of the power of authoritative interpretation by the state parties is just one of many tools to secure the “right balance” between private and public interests. Others relate to more clearly defining substantive standards or restricting or delaying access to investor-state arbitration. In particular, applying fresh thinking to a flexible exhaustion of local remedies rule appears to be central to preserving the “right balance” between private and public interests. Another tool some states have deemed appropriate to better preserve their policy space is to limit remedies in investor-state dispute settlement to monetary remedies. However, whether this instrument is indeed effective or rather counterproductive has yet to be critically assessed. Furthermore, since the interpretation of an investment instrument in investor-state arbitration, especially when containing novel clauses, can hardly be predicted, it is decisive to preserve some flexibility for future correctives and changes without having to renegotiate the whole agreement. Review periods and termination clauses specific to investment provisions and investor-state dispute settlement could bring this flexibility.

In any event, the EU and its institutions are well advised to carefully evaluate each of the inadequacies of investor state arbitration, thoroughly verify whether and to which extent they can be mitigated in a specific investment instrument and weigh them against the perceived virtues before subscribing to a particular model of adjudication; legacy alone should be no argument.

However, one illusion is to be warned against right from the outset: due to the current fragmented state of international investment law there is neither an easy nor a quick solution to the challenges posed.

Rather, it will take years – if not decades – to address them properly. Nonetheless, the EU as a major new player entering the “great game” of investment treaty making is presented with the unique opportunity to lay the foundations for a more predictable and balanced approach to protecting foreign investment and preserving sufficient policy space with the view to adequately addressing the puzzling regulatory questions of the future in a common interest. Thank you.

### 3. INTERNATIONAL INVESTMENT PROTECTION AGREEMENTS AND EU LAW

*by Dr Ingolf Pernice*

#### 3.1 General remarks

International Investment Protection Agreements (IPAs) must be recognized as an important step forward in international law to give international law more bite. Allowing for arbitration under an Investor State Dispute Settlement (ISDS) provisions with final awards to be enforced at whatever place in the world means **taking law seriously**. It provides investors with legal certainty and, thus, establishes a reliable foundation for some legal certainty and trust, which is a crucial condition for effective foreign investment.

It is also a step towards developing a global legal order **taking people seriously**. People from other countries would not depend entirely on the will of the sovereign in the host country; they are recognized as holding individual and enforceable (procedural) rights independently of the respective national system of judicial review, eventually even against what the actual government or legislator considers to be opportune. This is an important development, since – in contrast to international law in general – enforcement of rights against the host state under the IPA is not left only to the government of the country of origin and to diplomatic consultations between the two governments involved, but the individual concerned has her own legal standing.<sup>1</sup>

Yet, there are tensions between IPAs and the concept of **national sovereignty** in international law. While it is true that concluding international treaties is an expression of national sovereignty, rather than limiting it, this assumption is questionable if external bodies are given the power to assess and effectively sanction acts of the sovereign. A country party to IPA's may therefore be limited by such chilling effects in the democratic choice of its policies; the more foreign investment it has accepted, the more costly certain political choices may become, for the damages or compensation expected to be awarded by arbitral tribunals. Such financial risks may even amount to reach a prohibitive size.<sup>2</sup>

As a result, IPAs with ISDS-clauses must be drafted so as to ensure the legitimate rights of foreign investors and establish the level of trust necessary for economically meaningful investment, but at the same time strike a balance with the protection of the democratic and legal autonomy of each party, so to leave the enough leeway to articulate and implement policies pursuing in the name of national public interest. Such a balance seems to require that:

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<sup>1</sup> Divergent views on the question whether the rights in substance are those of the home country and only exercised by the investor, or the investor defends her own rights established by the IPA, will not be dealt with here. The general position seems to be that the questions are of an international law nature and, therefore, issues among states (see Ian Brownlie, *Principles of Public International Law*, 7th ed. (2008), pp. 519-551, where the key reference seems to be diplomatic protection, *ibid.* p. 519). The issues at stake, however – such as national treatment, international minimum standards, denial of justice, expropriation – relate to individuals, and it is difficult to deny that individual (procedural) rights are involved, at least when, by ISDS-clauses, the individual investor concerned is given legal standing for defending her property, legitimate expectations, access to justice etc.

<sup>2</sup> See on this Brownlie (note 1), p. 537, on nationalization which is possible if prompt and adequate compensation is paid: „In reality this renders any major economic or social programme impossible, since few states can produce the capital value of a large proportion of their economies promptly“.

- there is no discrimination of, nor privilege for foreign investors as compared to nationals or residents in general;
- legitimate expectations and rights of foreign investors as to the market conditions in the host country are honoured;
- state parties to the IPAs are not discouraged to articulate and implement democratically decided policies of public interest;
- if fundamental public interests and/or individual rights are at stake, dispute settlement must be public, transparent and organized through legitimate bodies.

### **3.2 Specific Questions regarding IPA's of the EU**

The abovementioned principles apply to states and to the EU accordingly. Nevertheless, the situation of the EU as a party to IPAs is of a specific nature. The EU is not a (federal) state and whatever investment is made within the EU takes necessarily place on the territory and, therefore, within the jurisdiction of at least one of its Member States. Two interrelated sets of norms, the internal law of that state and Union law are applicable. These peculiarities of the EU are to be kept in mind when discussing general issues of IPAs and, in particular, their ISDS-clauses.

Specific questions arise with regard to the competence and the responsibilities of the EU and the Member States, the scope of IPA's and their impact on national policies and freedom of action, and the direct effect of these agreements and their status in the national legal systems.

#### **3.2.1 EU competence to conclude direct investment treaties**

According to Articles 3 (1) (e) and 207 (1) TFEU and Articles 63-66 TFEU on free movement of capital within the EU and with third countries the EU has competence to conclude IPAs including ISDS-clauses with all possible implications on policy choices and, therefore, the exercise of democratic sovereignty at the national level.

#### **3.2.2 Scope of EU direct investment treaties and national competences**

The binding effect upon national policies is of a general nature, as IPAs do not distinguish among policy areas but just set criteria like non-discrimination, fair and equitable treatment, access to justice, etc.; these criteria may be applied, in a given case, equally to policy areas where the EU is competent to legislate (e.g. agriculture, environmental protection, consumer protection) and where Member States have kept their legislative autonomy (e.g. economic, fiscal, social, culture, education, health policies). Limiting effects of IPAs concluded by the EU on sovereign policies including the national level, therefore, may well touch upon policy areas that remain within the scope of national competence.

#### **3.2.3 Primacy and direct effect of EU direct investment treaties**

Under Article 216 (2) TFEU agreements concluded by the Union are binding upon the institutions and its Member States. According to the established case-law of the European Court of Justice (ECJ) they become an integral part of the Union legal order. Their provisions could, if the special conditions are met, be invoked against acts of secondary EU law to the extent that these acts are in conflict with them. More importantly, their provisions would take part in the principles of primacy and direct effect of Union law, even with regard to national constitutional law. This „overdrive“-effect the incorporation of international agreements into EU law brings about at the national level, of course, only applies if a direct effect is accorded to the substantial provisions of the IPAs.

### 3.3 Tensions between EU law and IPAs in general

While Member States concluding Bilateral Investment Agreements (BITs) prior to the entry into force of the Lisbon Treaty had to respect EU law and the agreements could not be enforced in case of conflicts without infringement to Union law, the situation is different for IPAs concluded with third countries by the EU. The EU and its courts will not be able to rely upon any claim of primacy for its own law over legal commitments it has taken in an international agreement. In other words: While legal conflicts of measures by Member States undertaken in accordance with their bilateral investment treaties on the one hand, but in breach of their duties under EU law on the other hand (e.g. state aids, consumer protection etc.), may well need a solution giving precedence to EU law over international obligations, no such argument can be accepted *a priori* regarding the international obligations the EU has agreed to.

Hence, where tensions may arise between general EU law and obligations under IPAs concluded by the EU, it is of highest interest for the EU to ensure that appropriate instruments to resolve such conflicts are found prior to the entry into force of such agreements in order to ensure that both EU and national public policies are not compromised by the risk of foreign investors preventing the measures deemed necessary, or claiming compensation.

Based upon the experience with existing agreements of the Member States the following problem areas can be identified:

#### 3.3.1 The “regulatory chill”

Depending on the interpretation given by the arbitral tribunals in confidential proceedings on provisions like fair and equitable treatment, etc., social policies like the introduction of minimum wages and the reform of the EU data protection regime may be jeopardized by proceedings initiated by foreign investors on the basis of the IPAs. Compared to the protection foreign investors benefit from in their home state, the practice of the arbitration tribunals seems to develop towards a “super-protection” in foreign countries, with adverse effects upon the host countries’ legislative autonomy. What might have been very much in the interest of capital exporting countries like the US, the UK or Germany in their relationship to third world countries needing investment during the last decades now turns back on EU Member States with unexpected legal risks against their own policies.

#### 3.3.2 The EU state aid regime

Where some incentives have been promised or implemented for attracting foreign money the investor may not be happy with the recovery of the aid, if ordered by the Commission under the state aid regime of the EU, and argue that it had rightfully trusted the government having promised or granted the aid. The investor may invoke fair and equitable treatment or other rights granted under the IPA and be accorded the amount equal to that of the state aid in compensation. The result is that Articles 107 and 108 TFEU could not effectively be applied and the distortions of competition in the internal market stated by the Commission to result from the unlawful aid cannot, finally, be excluded.

#### 3.3.3 The principle of non-discrimination

Foreign investors under IPA’s would have the same rights as Member States nationals regarding establishment, providing services as well as for participation in the capital of companies in other Member States as granted to nationals under Article 55 TFEU, including legal remedies. Foreign investors, however, could use the ISDS as a “fast track” procedure and be privileged compared to EU investors both in procedure as well as in substance, depending on what interpretation is given to EU law by the tribunal.

### 3.3.4 ISDS clauses and the autonomy of the Union's legal order

ISDS-clauses in an IPA concluded by the EU can raise problems for the autonomy of Union law and its interpretation. Similarly cases regarding clashes between European or national rules on the one side, and provisions protecting more or less legitimate expectations of foreign investors, etc. on the other side, may involve questions of Union law with regard to its interpretation and at times even its validity. As the arbitration tribunal would only assess whether or not the guarantees given to investors in that agreement are violated and, if so, declare the EU or a Member State liable for damages or compensation, the effect of such a judgment could reach beyond what is accepted under the WTO or ECHR systems. ISDS are made to give the investor directly enforceable rights. Even if the tribunal would not give a binding ruling on the interpretation or applicability of Union law, its decisions could well impact the functioning of the EU legal order and so considerably affect its autonomy.



### **3.4 Configuring IPAs in compliance with EU law**

With regard to the abovementioned problems of IPAs concluded by the EU with third countries the following solutions may be considered for ensuring compliance with the law of the European Union.

#### **3.4.1 Regulatory autonomy - overcoming the “regulatory chill”**

Given legitimate criticism against the “regulatory chill” by IPA commentators, the European Parliament and the Commission agree that the regulatory autonomy of all contracting parties must be guaranteed by an express provision in the agreement. The key problem with ISDS in this context seems to be the vagueness of the protection clauses. Given the adverse effects of ISDS, the best solution, therefore, would seem to opt for a more integrative solution, which would be designed according to what may be called the “European model”. As far as this proves politically undesirable or impossible, detailed provisions may be envisaged for the IPA aiming at more legal certainty regarding the preservation of the regulatory autonomy of the contracting parties.

#### **3.4.2 Repercussions of the “EU model” on the state aid regime**

Absent special protection for the foreign investor on the basis of equal treatment tensions with the EU state aid regime, as explained, can be avoided. Investors from third countries would be subject to the same obligations regarding aids granted by Member States as investors from any EU Member State. In the interest of legal certainty an IPA with ISDS-clauses should contain express references to the obligations under the EU state aid regime and to the procedures applicable, making clear that legitimate expectations may not be based upon commitments made by a national authority regarding the compatibility of a measure with state aid law.

#### **3.4.3 Securing respect for the principle of non-discrimination**

Giving the foreign investors a special remedy is exactly what the agreements with ISDS-clauses are about. This would not only discriminate against EU investors inside the EU but equally become an incentive for investors generally to invest abroad instead of within their respective countries. To ensure equal treatment effectively would need establishing a common legal system including directly applicable guarantees in substance and procedure, along the lines given by the model of the European internal market.

#### **3.4.4 Preserving the autonomy of the Union’s legal order**

To have no ISDS clause in an IPA would avoid any problem with regard to the autonomy of the EU legal order. The IPA would, however, lose one of its most important and effective elements. Thus, if the “EU model” suggested above is politically not available, it is necessary to design ISDS arrangements so to avoid implications giving reasons for concern that the autonomy of the Union’s legal order be negatively affected. Exhaustion of local remedies would ensure that the ECJ is involved when required. Another option could be to include into IPAs of the EU provisions on the establishment of a permanent court for the settlement of disputes under the IPA. To give such a court the right to refer questions to the ECJ under Article 267 TFEU, however, would need a teleological interpretation of Article 267 TFEU or an amendment of the Treaties. Another, “softer”, solution could be the model of the prior involvement procedure applied in Article 3(6) of the draft treaty on the accession of the EU to the ECHR. It would imply, however, a new competence of the ECJ and require prior amendment of the TFEU too.



### **3.5 One-size-fits-all or tailor-made solutions ?**

With a view to the diversity of the development both, economically and regarding good governance, individual rights, the rule of law and judicial protection there are doubts whether a one-size-fits-all solution is realistic. It seems, rather, to be appropriate to consider a “European model” solution for agreements upon free trade areas such as under the TTIP with the US or the CETA with countries having similarly developed systems of fundamental rights and judicial review. Cooperation with other countries could be developed upon the basis of agreements containing ISDS clauses of a “new generation” that make sure that national public policies are not jeopardised. Effective protection could be conditioned in such agreements by clauses making sure that the investors fully respect certain internationally agreed rules of behaviour, including the standards of corporate social responsibility (CSR).

### **3.6 Delaying or differentiating investor's access to ISDS**

At first sight, it is difficult to find reasons for differentiating among investors with regard to access to ISDS. Such differentiation could easily be understood as discriminatory. There are cases, nevertheless, where a differentiation should be seriously considered.

#### **3.6.1 Local remedies privilege**

If an investor has exhausted local remedies in the host country it may be justified to facilitate its access to the ISDS both, regarding procedure and regarding fees. Such a “local remedies privilege” would induce investors to accept the domestic judicial system as a first and hopefully effective remedy, it would also reduce the number of claims in the ISDS and so save costs and time for the contracting parties.

#### **3.6.2 Differentiation *ratione materiae***

It is appropriate to give investors privileged access to ISDS in cases of violation of the principle of fair and equitable treatment where access to justice in the host country is refused. The arbitration tribunal can order the re-examination of the matter by the domestic authorities or courts with penalties to be paid for any undue delay, or directly award adequate compensation to the investor for the failure of the national authorities of the host state to ensure fair and equal treatment. Similar preference could be considered for cases where the transfer of capital related to the investment is restricted. Such cases need rapid remedy, and there seems to be no major difficulty in assessing the legitimacy of a claim or of the measure put to scrutiny. For other cases such as compensation for direct or indirect expropriation or violations of the principles of national or most favoured nation treatment may be more difficult to judge, in particular where the regulatory autonomy of the host state is at stake. They could be subject to a two step procedure under which a claim to the arbitration tribunal is admissible only after a “special committee” to be established by the contracting parties has found that the claim under the ISDS is not abusive.

#### **3.6.3 Differentiation *ratione tempore* – urgency and interim measures**

Special attention should be paid to cases where a rapid decision by the arbitration tribunal or even interim measures can avoid greater damage. There should be an accelerated procedure upon request of the investor for such cases, if the “special committee” finds the request *prima facie* well grounded. However, the arbitration tribunal in charge may decide to deal with the case in normal proceeding if the reasons given for the accelerated procedure prove not to hold in substance.

### **3.7 Should there be an ad hoc tribunal or a standing court?**

Given the power of the ISDS tribunals to issue awards that may affect the regulatory autonomy of the contracting parties, legitimacy requirements are of utmost importance. It is the choice and the independence of the tribunal and of the arbitrators, it is the transparency of the proceedings, but it is also the visibility and stability of the institution to be held accountable for its case law what makes up legitimacy. If *ad hoc* tribunals with changing composition appear and disappear, if arbitrators are appointed *ad hoc*, after having worked as lawyers in other cases and before returning to other business when the case is decided, it will be more than difficult for the general public to hold them accountable, to assess the awards and to react to the performance of the system at large. With a permanent court, in contrast, some kind of jurisprudence will be developed within the framework of each agreement, that the judges have to stand for and on which basis some legal certainty may emerge progressively.

### **3.8 Access to ISDS, the local remedies rule and the role of a “special committee”**

The arbitration tribunal should be regarded as a solution of last resort only. As a consequence, access to ISDS should be subject to a compulsory attempt to reach settlement. With a local remedies rule the investors' protection could lose much of its effectiveness. It could only be admitted if there is a time limit giving the investor a right to pass on ISDS when no satisfactory decision was given by the national courts within that time. The optional form of a “local remedies privilege” would be the better solution. A “special committee” composed of one representative of each of the contracting parties and one of the arbitrators they may agree upon might be in charge of admitting investors for an “accelerated procedure” when good reasons are given for the urgency of the matter.

### **3.9 Preserving the autonomy and coherence of the Union's legal order**

Arbitration tribunals should be bound, in applying the provisions of the IPA, to abstain from giving its own interpretation to provisions of national or Union law but – under a prior involvement procedure or otherwise – endeavour to follow authoritative guidance from the ECJ or hear the European Commission – to be invited as *amicus curiae* – for obtaining information on how relevant Union law should be understood. Provisions to this effect should be included in the agreement on ISDS.

### **3.10 Transparency and access to information**

One of the fundamental requirements of legitimacy both for the negotiation process of IPA establishing ISDS and of the functioning of ISDS is transparency. Accordingly, the proposals of the Commission to provide for public access to information and documents related to ISDS proceedings shall be welcomed. It allows scrutiny and criticism by all interested parties and, thus, contributes to the legitimacy of the tribunals, academic analysis and, finally also to legal certainty for investors and states. In this vein, all arbitral proceedings under ISDS to which a Member State is party must be open to the public and its decisions be published.<sup>3</sup> It is only under the conditions of transparency that parliamentary control can take place effectively.

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<sup>3</sup> From a German constitutional law perspective arriving at the same conclusion Johanna Wolff, “Nicht-öffentliche Schiedsverfahren mit Beteiligung der öffentlichen Hand am Maßstab des Verfassungsrechts”, *Neue Zeitschrift für Verwaltungsrecht* 2012, pp. 205-209.

### **3.11 Public participation in the proceedings**

The same is true for allowing public participation in the proceedings, namely that, for instance, NGOs and civil society at large have an opportunity to submit their views.

### **3.12 Choice and deontology of the arbitrators**

Arbitrators in ISDS are exercising an enormous power, their choice and deontology must therefore be beyond any doubt. The current practice is opaque and all initiatives for introducing a transparent and rule-based system for the selection of arbitrators and for establishing a code of conduct for their activities must be welcomed. These rules could follow the system for selection of judges for supreme or international courts, if there is a standing court as suggested above; but even if a system of ad-hoc tribunals is envisaged, the list of persons available for participating in an arbitration tribunal should be established in a transparent and rule-based system excluding any conflict of interest and doubts about the integrity of the arbitrators.

### **3.13 Appeal mechanism**

With a view to give the public interest of the contracting parties a decisive role and to allow some control over the outcome of ISDS in a given case, it seems to be appropriate to provide for an appeal mechanism allowing a final review by the contracting parties of the awards given by the arbitration tribunal. There is no reason, though, to duplicate the arbitration-model. The review should rather be a matter for a joint committee composed by representatives of both contracting parties. Appeals should be open to be launched both, by the investor or by the respondent. Only if the joint committee comes to an agreement upon the incorrectness of the award, the award may be nullified and sent back to the arbitration tribunal with instruction about the agreed interpretation of the rules in question or, if there is no room for further consideration, be amended so as to comply with the authoritative interpretation given to the IPA by the contracting parties.

## DISPUTE SETTLEMENT RESOLUTION IN PRACTICE

by Ms Meg Kinnear



# An Introduction to ICSID Process

## Workshop on ISDS provisions in the EU's International Investment Agreements European Parliament

Meg Kinnear  
ICSID Secretary-General  
April 1, 2014

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## The World Bank Group

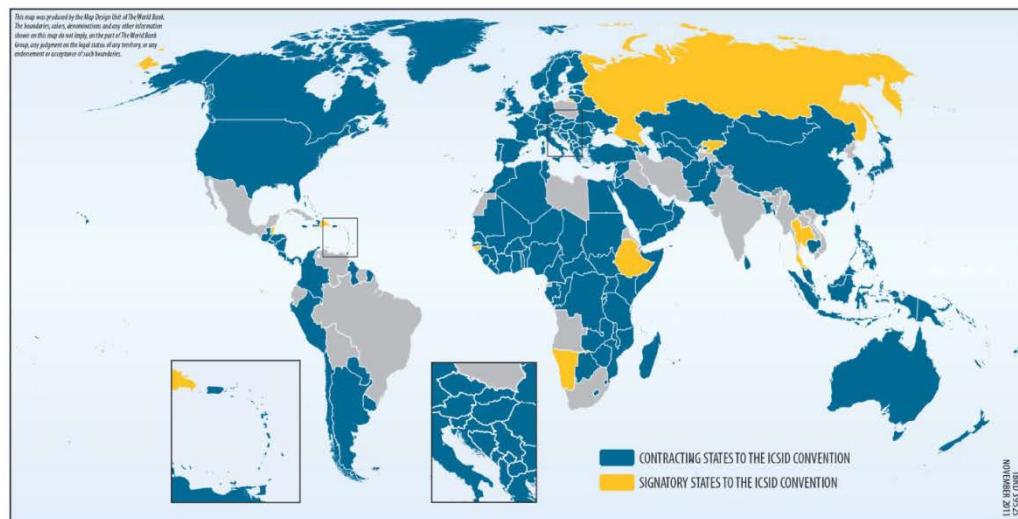


| ICSID   | IBRD  | IDA   | IFC  | MIGA   |
|---|---|---|--|--|
| International Centre for Settlement of Investment Disputes                                  | International Bank for Reconstruction and Development           | International Development Association   | International Financial Corporation  | Multilateral Investment Guarantee Agency                                       |
| <b>MISSION:</b>   | <b>MISSION:</b>   | <b>MISSION:</b>   | <b>MISSION:</b>  | <b>MISSION:</b>  |
| ➤ Provides facilities for conciliation and arbitration of international investment disputes | ➤ Lends funds to governments of middle and low-income countries | ➤ Provides interest-free loans and grants to governments of poorest countries | ➤ Provides loans, equity and technical assistance to stimulate private sector investment in developing countries | ➤ Guarantees for investors in developing countries against non-commercial risk |

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## ICSID Membership 150 Members



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## ICSID Proceedings

### Convention

(Both disputing parties from ICSID Contracting States)

- Conciliation
- Arbitration

### Additional Facility

(One disputing party from Contracting States)

- Conciliation
- Arbitration
- Fact-finding

### Other

(Need not be from Contracting State)

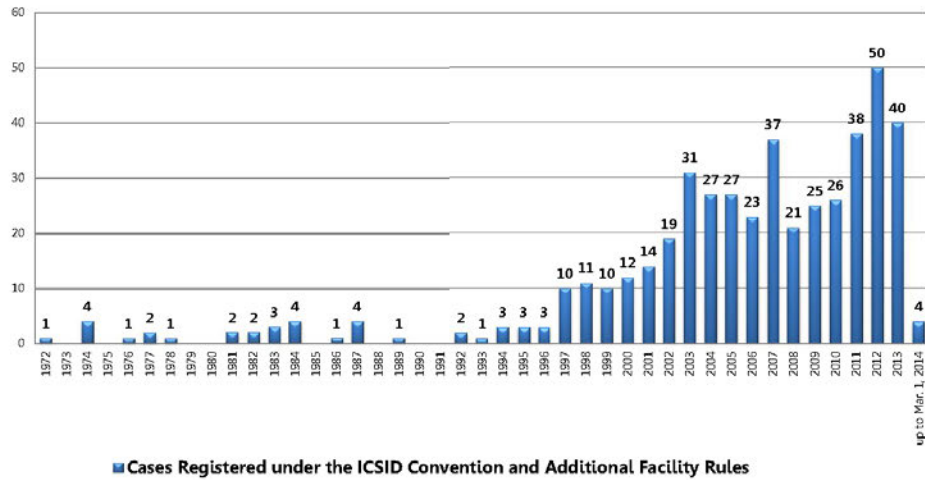
- **Case administration under other Rules or Treaties** (e.g.: UNCITRAL investment cases; State-to-State cases)
- **Other functions on consent of parties** (e.g.: Fact-finding, Mediation)

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## ICSID Caseload – March 1, 2014

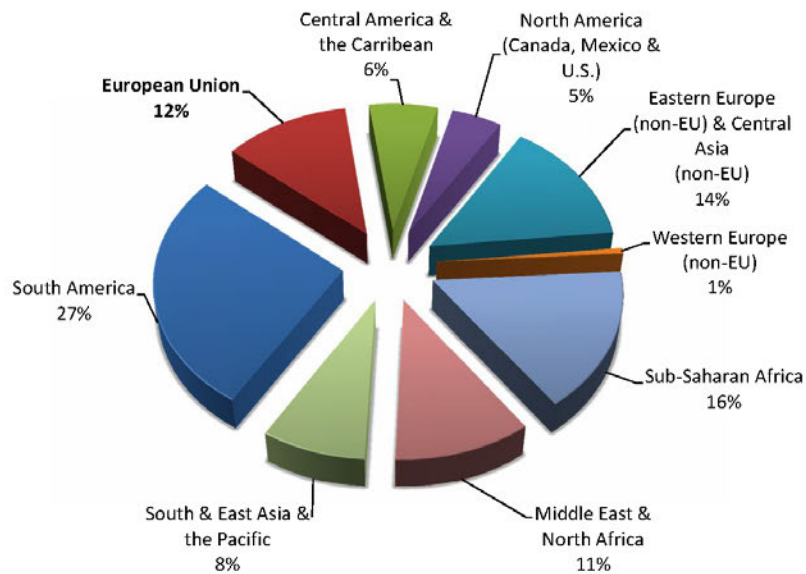


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## ICSID Cases by State Party – March 1, 2014



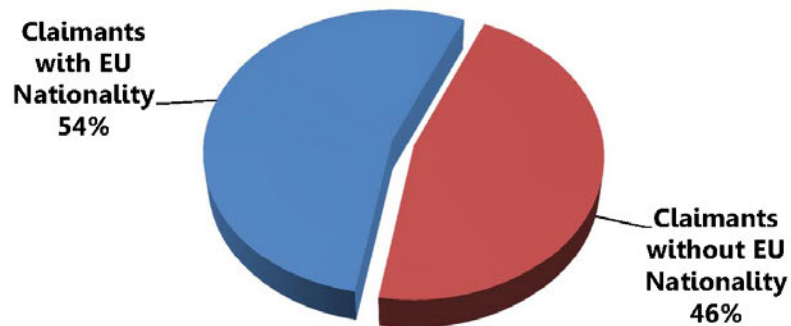
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## ICSID Cases by Claimant Nationality – March 1, 2014



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## Consent is the Cornerstone of Jurisdiction

Sources of Consent:



- Contracts
- Investment Laws
- Bilateral Investment Treaties
- Multilateral Agreements

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8



## Conduct of an ICSID Convention Case



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# Transparency - Procedural Details

## Procedural Details

**Fraport AG Frankfurt Airport Services Worldwide v. Republic of the Philippines**  
(ICSID Case No. ARB/11/12)

| Original Arbitration Proceeding |  |
|---------------------------------|--|
| Date                            | Development  |
| April 27, 2011                  | The Secretary-General registers a request for the institution of arbitration proceedings.  |
| June 27, 2011                   | Following appointment by the Claimant, Stanimir Alexandrov (Bulgarian) accepts his appointment as arbitrator.  |
| July 29, 2011                   | Following appointment by the Respondent, Albert Jan van den Berg (Dutch) accepts his appointment as arbitrator.  |
| February 06, 2012               | Following appointment by the parties, Piero Bernardini (Italian) accepts his appointment as presiding arbitrator.  |
| February 07, 2012               | The Tribunal is constituted in accordance with Article 37(2)(a) of the ICSID Convention. Its members are: Piero Bernardini (Italian), President, appointed by agreement of the parties; Stanimir A. Alexandrov (Bulgarian), appointed by the Claimant; and Albert Jan van den Berg (Dutch), appointed by the Respondent. |
| April 03, 2012                  | The Tribunal holds a first session in Washington, D.C.   |
| April 18, 2012                  | The Respondent files a written submission on preliminary matters.  |
| May 02, 2012                    | The Claimant files a written response to the Respondent's submission on preliminary matters of April 18, 2012.   |
| May 17, 2012                    | The Tribunal issues a Procedural Order No. 1 concerning preliminary matters.   |
| August 17, 2012                 | The Claimant files a memorial on liability.  |
| November 19, 2012               | The Respondent files a counter-memorial on the merits and a memorial on jurisdiction, including counter-claims.  |
| January 07, 2013                | The parties file requests for the Tribunal to decide on production of documents.   |
| January 18, 2013                | The Tribunal issues a decision on production of documents.   |

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## Transparency – Other Provisions

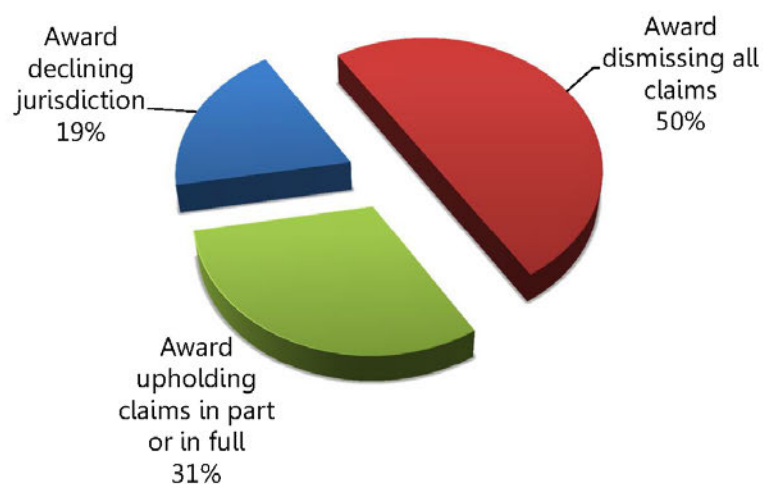
- Publication of awards
- Open hearings
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- Can apply the new UNCITRAL Transparency Rules if treaty requires or parties agree

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## Disputes Decided By Tribunals – EU MS Respondents - March 1, 2014



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1818 H Street, N.W.  
Washington, D.C. 20433  
USA

Tel: + 1 (202) 458-1534

Fax: + 1 (202) 522-2615 or 522-2027

Website: [www.worldbank.org/icsid](http://www.worldbank.org/icsid)

## PART III: SUMMARY OF THE WORKSHOP

*by Elfriede Bierbrauer and Charlotte Moelgaard (intern), Policy Department*

The workshop on investor-state dispute settlement (ISDS) provisions in the EU's international investment agreements raised some important points. This summary presents the arguments made in four parts. Part one illustrates why ISDS provisions are essential, not least for the EU. Part two discusses possible challenges to these provisions. Part three shows in detail how ISDS provisions in international investment agreements could be outlined in an EU context. In part four, an overview of the discussion following the introductory statements concludes the summary.

### 1. OBJECTIVE

The EU, with its stock of investment totalling more than EUR 7 trillion, is a leader in global foreign direct investment (FDI). Investments are important for economic growth, job creation and development in the Member States. For more than 50 years, outward investments from, and inward investments into, the Member States have been accompanied by more than 1200 individual bilateral investment agreements with partner countries.

Professor Vital Moreira, Chair of the Committee on International Trade (INTA), introduced the subject with reference to the Lisbon Treaty, which had brought FDI under the exclusive remit of the EU, thereby creating an opportunity for integrating more comprehensive investment provisions in the EU's trade agreements. Parliament has supported a strong EU investment policy from start, calling for EU investment agreements gradually to replace Member States' agreements with third countries and drawing attention to several elements in which the existing system could be improved, substantially as well as procedurally. In its resolution of 6 April 2011 on the future European international investment policy<sup>4</sup>, Parliament, *inter alia*, took the view that ISDS is an important element of investment agreements, but noted some perceived negative aspects of ISDS and called on the Commission to address these while negotiating agreements on behalf of the EU. Since then, the Commission has been negotiating investment agreements with a wide range of countries, both in the form of investment chapters in FTAs with Canada, ASEAN, Japan, US, etc., and as a stand-alone investment agreement with China.

While neither investment protection agreements nor ISDS are a novelty for the Member States, it is only recently that they have received public attention, in particular in the context of the EU-US negotiations for the Transatlantic Trade and Investment Partnership (TTIP). It is in this context that the workshop was organised, providing a forum to discuss why such agreements and dispute settlement systems exist in the first place, how they have been used, and what the most critical aspects of these are, as well as to air the advantages and disadvantages of ISDS provisions.

With reference to the Lisbon Treaty, European Commission Director Rupert Schlegelmilch recalled that the competence for foreign direct investment has been transferred from the level of the Member States to that of the EU. This means that the EU plays an important role in international investment protection, including investment dispute settlement. The need for appropriate ISDS provisions in the EU's international trade and investment agreements is therefore apparent. With this enlarged competence, the EU, as an international actor, will face new challenges in this field. At the same time, this should also be seen as an opportunity to address these challenges by means of a new approach, not least because doing nothing is not an option (as it would mean that the agreements negotiated by the Member States – the focus of public criticism – would remain in place). In this regards, the Commission has made

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<sup>4</sup> Texts adopted, P7\_TA(2011)0141.

efforts not only to ensure the right balance between high standards of protection and the right to regulate in bilateral negotiations (in which context Canada was mentioned as an example to follow), but also to pursue this agenda on the international stage (in particular by having the EU take a leading role in the work to improve the transparency rules of the United Nations Commission on International Trade Law (UNCITRAL)).

This view was reiterated by Professor Steffen Hindelang, who added that, as a new player, the EU – and the European Parliament in particular – had the opportunity of challenging the existing approach and creating a more predictable and balanced dispute settlement mechanism for the future. Since the 1970s, almost all bilateral and regional investment agreements had provided for ISDS, and ISDS provisions in international investment agreements had provided foreign investors with a tool with which to commence international arbitration against host states where administrative, regulatory or judicial measures had led to direct or indirect expropriation, discrimination or other adverse treatment.

Professor Pieter Jan Kuijper addressed the topic by looking at the history and objectives of bilateral investment treaties (BITs). He pointed out that while the original purpose of BITs was to attract foreign capital to developing countries in order to stimulate their economic development, today such treaties were increasingly concluded between parties at similar levels of development. At the end of 2013, almost 3000 BITs had been concluded worldwide. The usual elements of BITs included provisions on conditions of access, national treatment, most-favoured nation treatment, minimum standard of treatment, and fair and equitable treatment. Furthermore, there were investment protection clauses which foresaw the free transfer of funds, protection against nationalisation, and compensation as well as dispute settlement clauses, including ISDS. ISDS provisions made it possible for an investor to bring a case to an ad hoc tribunal without having to rely on the government to espouse the claim. By moving away from the state-to-state dispute settlement framework, the ISDS also removed politically inspired restraints on launching investment claims. Prof Kuijper also touched on the position of BITs in the framework of the World Trade Organisation (WTO), and on related regulations such as those pertaining to international investment and trade law as stipulated by the Agreement on Trade Related Investment Measures (TRIMS), investments in the service sector under the General Agreement on Trade in Services (GATS), and intellectual property (IP) rights under the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs).

As Professor Hindelang stated, the grand idea behind ISDS provisions was to provide a safety net that limited government arbitrariness in order to ensure a greater level of impartiality in dispute settlements. However, as explained by Professor Ingolf Pernice, the more foreign investments were accepted, the more costly political choices could become for the host state. He emphasised that investment protection agreements (IPAs) and ISDS-clauses must be drafted in such a way as to ensure the right balance between, on the one hand, the rights of foreign investors – thereby creating a legitimate level of trust for investments to take place in the first place – and, on the other, the regulatory autonomy of the host state.

Ms Meg Kinnear, Secretary-General of the International Centre for Settlement of Investment Disputes (ICSID), showed how the number of cases in investment disputes had increased to more than 560 cases by the end of 2013. Though established in 1966, most of cases brought before the ICSID had been filed in the past 15 years. As of 1 March 2014, 12 % of all ICSID cases concerned an EU Member State, while 54 % of all claimants were from the EU, making European investors the biggest users of ISDS. Ms Kinnear explained that 55 % of ISDS cases before the ICSID – a majority – had been settled in favour of the state and only 45 % in favour of the investor. With regard to disputes that had been decided by tribunals, and in which EU Member States had been the respondents, 19 % of the awards had declined the claim on grounds of jurisdiction, 50 % had dismissed the claim completely, and only 31 % had

supported the claims in part or full (whereas even in these cases the rewards amounted to, on average, 35-40 % of the claimed amount).

## **2. CHALLENGES**

Professor Hindelang pointed out that while a growing numbers of investment agreements were in force, some countries have not renewed their investment treaties, and a small number of countries have withdrawn completely from the current system. While there was no easy or quick solution for the EU to the challenges that ISDS presented, Professor Hindelang stressed that significantly weakening or even completely renouncing ISDS would not be an option.

According to Professor Pernice, the EU would not be able to claim any primacy of its own law over legal commitments made in international agreements. The European Court of Justice (ECJ) does not accept challenges to the autonomy of the Union legal order. While arbitration tribunals could judge cases involving EU law, they would be unable to submit questions to the ECJ, and while such tribunals would interpret investment agreements according to international law and not EU law, their decisions could still lead to tensions in some areas, such as those pertaining to the EU internal market or to state aid. At the same time, foreign investors using ISDS as a 'fast track' could be seen as enjoying a privilege not available to their EU competitors. In order to protect investors in a way that takes on board the views of NGOs and the general public, new solutions needed to be found. Professor Pernice also pointed out that, at a more 'local' level, friction could arise with regard to the division of competences within the EU: IPAs and ISDS clauses were general in nature, and could thus interfere with policies in areas in which the Member States have maintained their autonomy. In addition, public criticism of the lack of transparency in investment disputes had increased the relevance and importance of changing practices in this regard with a view to regaining public support and trust. In sum, the EU could not simply begin to engage with these ISDS provisions without addressing these potential conflicts and seeking ways to resolve them.

## **3. CHARACTERISTICS**

While investor protection is manifest and essential for the EU economies, it is no secret that the EU is specific in nature: it does not function like a federal state, as underscored by Professor Pernice. The EU needed to consider all aspects of engaging in investment disputes if conflict between EU and international law were to be avoided.

Director Schlegelmilch explained that the EU was seeking to improve both the substantive rules and the procedure for enforcing these rules (arbitration). In substance, the efforts included: enforcing the 'right to regulate' principle; clarifying what 'indirect expropriation' includes (underlining that a measure of general application could not be considered as such, unless it is manifestly excessive); banning shell-companies (companies without a substantial economic presence in the EU) from channelling complaints; and providing a clear definition of 'fair and equitable treatment' as, primarily, a way of ensuring due process and stopping government harassment. On the procedural side, consideration would be given to provisions on: mandatory transparency; the impartiality and ethical conduct of arbitrators (to be guaranteed by an ethical code of conduct, a roster of arbitrators, etc.); the clarification of, and the placing of limits on, the powers of arbitrators; a ban on parallel claims ('treaty shopping'); making the loser of a dispute pay; and making it clear that it would be possible to sue for compensation but not to seek to rescind the law.

Professor Pernice also brought several specific suggestions on how the EU should approach the task of facilitating ISDS-clauses and potential dispute settlements. This included the creation of a permanent court, a 'special committee' and an appeal mechanism. Ad hoc tribunals would not serve the purpose,

as such arbitrators would likely not provide the transparency and stability wanted for such an institution. Also, given that tribunals would be considered a last resort, the 'special committee' should serve as a forum in which parties could meet before turning to a tribunal. As for the appeal mechanism, this new addition would allow for the parties to make a final review. Transparency had so far been a limited issue in investment dispute cases, as it had been possible to settle disputes without public scrutiny or access to information. This would no longer be the case.

Director Schlegelmilch also emphasised that provisions on transparency would have a given place in any future EU investment dispute settlement, as it already did in many ICSID and UNCITRAL cases. As Ms Kinnear confirmed, ICSID cases before independent arbitration tribunals would only be made public if both parties agreed to it.

So far, public interests in investment disputes had not been sufficiently accommodated. Professor Hindelang emphasised that the EU could and should preserve the virtues of the system (the management of political risk, the promotion of the international rule of law, the depoliticisation of individual investments, etc.) while reacting to criticism (by carefully defining terms, ensuring the right balance between private property protection and public interests, addressing the question of 'de facto precedents', publishing arbitration rulings and providing interpretation guidance). The EU had a unique opportunity to lay down a balanced and improved approach. The experience of the North American Free Trade Agreement (NAFTA) is one which the EU could reflect critically on and draw conclusions from. This would not only mean securing an acceptable outcome in treaty negotiations with other states; the EU would also have to ensure that the balance struck would not be distorted in subsequent dispute settlements, i.e. it would have to keep tribunals from turning into self-styled hidden law makers. 'Authoritative interpretation', the principle that state parties have the 'last word' on the meaning of investment provisions, would be an effective tool but should be used more proactively to prevent distortion of the balance initially struck by state parties.

Professor Pernice added to this by arguing for tailor-made solutions that ensured as well that national public policies would not be jeopardised in international disputes. While this carried the risk of being seen as discriminatory, it should be considered as a means of ensuring the protection of all parties.

## **4. DISCUSSION**

The individual statements by the presenters were followed by a discussion with Members and others attending the workshop. One Member showed an interest in the kinds of cases that had arisen in investment disputes, and asked how one can avoid uncertainties in this context and what the option for appeal were. Ms Kinnear referred to ICSID's experience in this regard, noting that cases had arisen in all sectors, including oil and gas, energy, mining, forestry, agriculture, construction and infrastructure management, telecommunications, financial services, tourism, the provision of water, waste management and media. The energy sector in particular had been the focus of disputes involving the Member States. Ms Kinnear added that, at present, there is no appeal option in these cases, only annulment. In response to this, the Commission representative and other experts said, in full agreement, that certainty and predictability could only be reached on the basis of clearly formulated texts in investment chapters, and/or in investment agreements, that do not leave room for too much interpretation ('the rulings of courts are as good as the rules that apply') and by having binding interpretations instead of de facto precedents. They also underscored the importance of preventing frivolous claims (by introducing 'loser pays' rules, etc.), avoiding 'cherry picking' and having it clearly stipulated that the host government's policy space is not to be encroached upon.



Another Member raised the issue of the process of selecting arbitrators in an EU context. The Commission representative replied by saying that, among other measures, Parliament would be consulted on the roster of arbitrators, though not on individual appointments.

One Member, while questioning the need for ISDS, regarded it as indispensable to modernise the ISDS mechanism and to develop it further in order to align it with a changing world. With reference to the proposed text for an ISDS clause to be found in the Commission's public consultation paper on the TTIP investment chapter, the Member also asked for confirmation that this text was identical to the one to be included in the future Comprehensive Economic Trade Agreement (CETA) with Canada. The latter was confirmed by the Commission representative.

One Member noted that it seemed obvious that current ISDS practice had been inspired by agreements with developing countries, and asked whether there was any data on investments that have not occurred because of a weak legal system. Other Members asked whether an ISDS clause was also needed for agreements between OECD countries, and, if so, why. Professor Kuijper responded by stating that one could not consider strong legal systems as the only ground for an investment decision. In strong judicial systems, the process could, for some, be considered too slow, or too bureaucratic, etc., hence investments in weaker systems still occurred. With regard to different clauses for different partners, Professor Pernice argued that there should be different solutions for the US and, e.g., China – a position not shared by the Commission, however: recalling that FDI would no longer follow a one-way street, Director Schlegelmilch pointed out that investment flows were now global. As the EU was increasingly witnessing inward investments, the ISDS provisions should be no different when dealing China than when dealing with the US. Last but not least, the Commission representative recalled that international law obligations would not be directly enforceable without the arbitration mechanism, and that even developed legal systems could have (and have had) biased policies that could raise very sensitive political issues if addressed in any other way.

Professor Hindelang, in reply to a question from a business stakeholder on whether an investor should exhaust the domestic legal system before turning to international law, noted that investors were not primarily interested in which law (international or local) applied, but were rather focused on having their disputes resolved in a satisfactory manner. Domestic courts, at least in advanced systems, could operate in a legal environment that was more consistent and predictable than current ISDS practice. Also, in contrast to the current ISDS model, it would be possible to correct erroneous decisions through the appeals mechanisms. When states were worried that investment tribunals did not pay sufficient attention to public interests, domestic courts could be better suited to take a first shot. Domestic courts were experienced in considering an investment case against the background of the whole domestic legal system. This system mirrored the elaborated, complex and refined balance of private and public interests agreed in the host state. Of course, the possible benefit of taking recourse to domestic courts before resorting to investment arbitration could vary significantly across national jurisdictions. Therefore, flexible and creative approaches were needed here as well.

Concern was also expressed as to whether the entire debate on investment disputes and ISDS provisions was pursued with the interests of large companies in mind. The Commission representative emphasised that, quite to the contrary, the aim was to make it even easier for small and medium sized enterprises (SMEs), by lowering costs (one arbitrator possibility) and by providing for mediated and/or facilitated dispute settlement procedures that accommodated smaller businesses in a better way, etc.

Following up on the introductory statements, a civil society representative expressed concern over whether and, if so, how EU law and international law could be combined. In reply, it was emphasised that this would depend on how the tribunals and the other facilities in question were to be framed. Professor Pernice argued that EU law could not be combined with ad-hoc tribunals established on the

basis of, and applying, international law. He argued for another solution so that all parties would be protected.

Representatives of US business organisations highlighted that the TTIP should be furnished with strong investment provisions for market access and investment protection, including ISDS, recalling that also the BIT model used with the US had undergone a substantive evolution. Furthermore, a TTIP with a modern ISDS clause would be well suited to set the standard for other, future agreements concluded by the transatlantic partners with third countries.

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