Will 2018 Mark a Tipping Point for Binding Investor-State Arbitration?

Kluwer Arbitration Blog
October 31, 2017

Colin Trehearne (Herbert Smith Freehills)

Please refer to this post as: Colin Trehearne, 'Will 2018 Mark a Tipping Point for Binding Investor-State Arbitration?', Kluwer Arbitration Blog, October 31 2017, http://arbitrationblog.kluwerarbitration.com/2017/10/31/will-2018-mark-tipping-point-binding-investor-state-arbitration/

The international economic order is today bound together through a network of bilateral (and multilateral) investment treaties which provide investors with a variety of protections. Such Bilateral investment treaties ("BITs") are a relatively young species dating back to 1959's Pakistan-Federal Republic of Germany BIT. While the exact content of BITs varies by agreement, most contain binding investor-State dispute settlement ("ISDS") pursuant to which investors of one State party to an agreement are able to bring arbitral claims directly against the investment-receiving host State (without the need for their home State to act, as was historically the case). From the investor's perspective, effective dispute settlement is a clear boon: it helps to increase levels of predictability and certainty by ensuring that the host country (receiving the investment) abides by its obligations under the BIT. ISDS was also designed to provide investors a fair hearing, free of politics, and before an independent tribunal. Like all arbitration, ISDS was also seen as creating enforceable decisions through a customizable and inexpensive process.

By their nature, bilateral agreements focused on the protection and promotion of investments were of interest to developed States. Developed States were generally capital exporting, had well-developed legal systems, and had the capacity to analyse, develop, and conclude BITs. Developed States were also, importantly, less likely to face the claims of investors. Over time the trend of BIT creation changed course and in the 2000s developing States too began demonstrating an independent interest in concluding BITs. By 2005 the United Nations Conference on Trade and Development (UNCTAD) was hailing a proliferation in global 'south-south' investment agreements developing alongside 'north-north' and 'north-south' agreements. States seemed to be of one mind that BITs were a desirable tool of policy: before 2012 only three BIT terminations had ever been declared and a 2015 OECD study found that States have rarely terminated, by agreement or unilaterally, investment treaties. With nearly 3000 BITs concluded (and with hundreds of other treaties containing investment provisions) there was little reason to question the continued existence of ISDS. Little reason, that is, until of late.

The international community today faces a unique moment in which ISDS may be exceptionally vulnerable to challenge. This is possible for four reasons. First, the number of BITs in effect has been under pressure due to recent terminations (including some bilaterally agreed terminations) by developing states. As some developing states have turned against ISDS, recent years have seen threatened, planned, or completed BIT terminations announced by, amongst others: Indonesia, Argentina, Poland, India, South Africa, Ecuador, Bolivia, and Venezuela. Although the reasons underpinning this varies by State, many seem likely to be motivated by a combination of recent record high numbers of investor-State disputes being filed and the regularity with which some of

these States face claims. The number of new agreements being concluded has also seen a significant slowdown since reaching a peak in the 1990s. According to UNCTAD data, the number of BITs concluded in 2016 (18) was the smallest number in about three decades.

Second, in light of the initial validity periods and related terms of many BITs, UNCTAD has estimated that by the end of 2018 there will be approximately 1600 BITs that can be terminated or renegotiated at any time. This is approximately 70% of all BITs presently in force and a significant number of these – at least 350 – will reach the end of their initial durations between 2014 and 2018. Although some States (including Japan, South Korea, and China) have continued to conclude new trade and investment agreements, a majority of bilateral investment treaties are now vulnerable to change. Third, some parts of civil society have begun questioning different aspects of BITs and in particular, the ISDS provisions. Such critiques (leveled too at the TTIP and TPP) tend to focus on perceived legitimacy, transparency, cost, and potential impacts on state regulatory powers. While such critiques are not unanswerable they have contributed to the emergence of the fourth (and most important, most uncertain, and most recent) reason 2018 may mark a tipping point: some major developed States – those that have long driven the development of BITs and ISDS – also appear to be questioning the merits of ISDS.

The United States, European Union, Canada and Australia represent just shy of 50% of world GDP; they have also all recently expressed opposition in some form to ISDS. In the United States, the U.S. Trade Representative, Robert Lighthizer, said in Senate testimony that he was "*always troubled by the fact that nonelected non-Americans can make the final decision that the United States law is invalid.*" While the US supported including ISDS in the Trans-Pacific Partnership (and continues to include it in its model BIT), media reports of the first round of NAFTA renegotiations suggested the US was considering an 'opt-in' system under which NAFTA member States would individually choose whether or not to allow investors of other States to bring ISDS claims. The position of the Trump administration on this point remains unclear but skepticism also has been visible amongst some Democrats and some Republicans. The EU, for its part, has recently said (in the context of its drive towards a multilateral investment court) that "*[f]or the EU ISDS is dead*" and that "*[u]nder no conditions can old-style ISDS provisions be included*" in the new EU-Japan Economic Partnership Agreement.

Some middle powers, developed but historically dependent on trade, have also joined this trend. Canada agreed to the EU's desired multilateral investment court, rather than ISDS, in the newly concluded EU-Canada Comprehensive Economic and Trade Agreement and the Canadian Foreign Affairs Minister later described this and other changes as examples of the kind of "*progressive*" trade deal Canada wants NAFTA to become. For its part, Australia has recently had a government that refused to accept ISDS provisions in new trade agreements and 2016's general election saw the largest opposition party publicly opposed to including ISDS provisions in future agreements. When coupled with certain developing States terminating BITs and refusing the inclusion of ISDS in future agreements, a majority of the world's economy is now overseen by governments either wary of, or openly opposed to, ISDS. In circumstances where roughly 70% of BITs will soon be able to be renegotiated or terminated, 2018 seems a crucial year for both opponents and proponents of investor-state arbitration to make their respective cases to maintain, reform, or abandon today's ISDS system.

The views expressed are those of the author.