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The EU Proposal Regarding Investment Protection: The End of Investment Arbitration as We Know It?

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On 12 November 2015, the European Commission rendered public and put on the negotiation table with the United States a proposal regarding the investment chapter of the draft Transatlantic Trade and Investment Partnership between the EU and the US (***TTIP***) (the EU Proposal). The text contains tentative remedies for major current criticisms against investment arbitration: the restriction of States' general regulatory power, the expansion of frivolous claims, the lack of transparency, the existence of conflicting awards and the appointment of arbitrators who are in conflict of interest situations. The remedy for the two latter criticisms is the establishment of a permanent court to hear investment disputes (***the Investment Court***). Is this proposal the trigger of major changes in investment arbitration, as we know it? This post will point to the main innovative features of the investment chapter of the EU Proposal, first regarding investment protection, and then regarding dispute resolution, especially the controversial creation of the Investment Court.

Investment Protection

Safeguarding States' power to regulate: Article 2 of the EU Proposal clarifies that the provisions on investment protection shall not affect the right of States to regulate in order to achieve legitimate policy objectives, such as the protection of consumers. The article specifically protects the right of States not to issue, or to discontinue, a subsidy, in the absence of any specific commitment to the contrary – and clarifies that "subsidy" includes "State aid" as defined in EU law. This provision clearly aims at addressing the issue that arose in the Micula arbitration, in which the tribunal found that Romania frustrated the Claimants' legitimate expectations and violated its fair and equitable treatment (***FET***) obligation by revoking, in the context of its accession to the European Union, subsidies incompatible with EU law.

Clarifying the notion of FET standard and expropriation: Article 3, which is an almost verbatim reproduction of Article X.9 of the EU-Canada Comprehensive Economic and Trade Agreement (the ***CETA***), details the situations amounting to a breach of the FET standard, as developed in international jurisprudence. Article 5 and Annex I (again very similar to relevant provisions of the CETA) offer detailed guidance on the notion of direct and indirect expropriation and the calculation of compensation, while clarifying that State measures protecting public health, environment, cultural diversity etc. do not constitute indirect expropriation except in the rare

circumstances when those would be manifestly excessive in light of their purpose.

Excluding a breach of a State's obligations in the event of a negotiated restructuring of public debt: Annex II prevents claims that a public debt restructuring amounts to a breach of the State's obligations as long as the debt restructuring is a negotiated settlement. This provision also exists in the CETA. In the midst of an economic crisis affecting several EU Member States, the EU is keen on protecting its members against arbitrations such as in Postova Banka v Greece or the very recent Laiki Bank v Greece cases.

Dispute Settlement

The establishment of a two-instance Investment Court: The EU Proposal provides for a Tribunal of First Instance (Article 9) and an Appeal Tribunal (Article 10) for investment disputes falling under the scope of the TTIP. Both tribunals will be composed of a fixed number of judges: in principle fifteen for the Tribunal of First Instance and six for the Appeal Tribunal, appointed for a six-year term. One-third of the judges must be nationals of the US, one-third nationals of an EU Member State, and one-third member of a third country. The criteria for the selection of judges (Articles 9.4, 10.7 and 11) are particularly strict. Judges must notably possess the qualifications required in their respective countries for appointment to judicial office and must refrain from acting as counsel, party-appointed expert or witness in any pending or new investment protection dispute. In practice, the last requirement excludes arbitration practitioners from appointment. This is not necessarily a good thing, given arbitration practitioners' expertise in investment arbitration law and their wide experience in investment arbitration cases. More generally, a closed list may only be a good list when political considerations have not interfered with its establishment. In the case of the EU Proposal, it is unclear how the judges will be selected.

The **dispute settlement procedure** provided in the EU Proposal is largely familiar from investment arbitration. Particular characteristics are the following:

– At any stage, the parties may initiate a mediation process (Article 5).

– If the investor is a US national the investor shall request that the European Union determine who is the respondent (EU or EU Member State).

– The investor may choose that the dispute be settled in accordance with the ICSID Rules, the Additional Facility Rules or the UNCITRAL rules – unless both parties agree on a different set of rules – and always subject to the provisions of the EU Proposal (Article 6).

– An appeal against the "provisional award" of the Tribunal of First Instance may be filed with the Appeal Tribunal.

– The President of the Tribunal of First Instance / of the Appeal Tribunal (drawn by lot among the judges who are nationals of third countries) appoints the arbitrators on a rotation basis, "ensuring that the composition of each division is random and unpredictable". Especially with regard to the Appeal Tribunal, the room for unpredictability is rather restricted given that it consists in principle of only six members, two of each category (US, EU and third-country nationals).

– An appeal can be based on the grounds of Article 52 of the ICSID Convention or if the Tribunal: (i) erred in the interpretation or application of the applicable law; or (ii) manifestly erred in the appreciation of the facts. The introduction of an appeal mechanism in investment arbitration is a

current trend. The ICSID Secretariat has worked on a possible appellate mechanism, and the 2015 UNCTAD Report also advises in favour of an appellate mechanism. The risk that the specific formulation of the EU Proposal entails is that grounds for appeal such as simple error in the interpretation and application of the law, or manifest error in the appreciation of facts (NB that national law is considered as fact in investment arbitration) are too wide and leave the door open for systematic appeals. Although Article 29 provides that the decision on appeal must be issued within six months, this seems rather unrealistic if the Appeal Tribunal has to re-examine the facts of the case.

Combatting frivolous and abusive claims and treaty shopping: Article 14 of the EU Proposal provides that the tribunal may dismiss a claim by a claimant who has already submitted claims arising out of the same facts to the tribunal or other fora. Moreover, Article 15 prevents treaty-shopping by providing that the tribunal shall decline jurisdiction where it appears that the claimant acquired ownership or control of the investment for the main purpose of submitting the claim. Finally, Article 28 provides that costs will be allocated following the "costs follow the event" principle. These provisions are very welcome in investment arbitration. On the other hand, the EU Proposal does not provide, as does the newly-published Trans-Pacific Partnership among Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the US and Vietnam (the TPP) for states to submit counterclaims, a measure which could also be efficient in limiting frivolous claims.

The EU Proposal also clarifies that class actions are not admissible (Article 7.5). The ability to hear collective claims under investment treaties has been controversial following the landmark Abaclat v Argentina award on jurisdiction of 2011, in which the tribunal upheld jurisdiction over the claim of around 60,000 bondholders.

Enhanced transparency: The Draft Proposal is perhaps the first international investment agreement that provides for the application of the UNCITRAL Transparency Rules (Article 18). Taking a step further, the Draft Proposal provides that all exhibits must be included in the list of documents specified in Article 3(2) of the UNCITRAL Transparency Rules. The EU Proposal also provides that parties must disclose the name and address of third party funders (Article 8).

The next steps: The EU Proposal will now be put on the US negotiation table. Following the negotiations, the final text will be incorporated into the TTIP. It remains to be seen whether the final version of the TTIP will be closer to the EU Proposal or to the recently published TPP, which is itself similar to the US Model BIT. What are the chances that the final TTIP provides for the establishment of an Investment Court? The fact that the TTP provides for investor-State arbitration as we know it may indicate the US's reluctance to experiment with alternative ISDS methods. Most importantly, the establishment of an investment court is not a simple matter. Several issues will have to be dealt with, before the introduction of the new mechanism: the relationship between the Investment Court and European courts, the status of its decisions when enforcement is sought outside the EU and the US, and so on.

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