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ISDS In The TPP: Is The Recent Uproar In The US Merited? – Part I

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In recent weeks, it has become clear that the latest lightning rod for TPP criticism is the Investor-State Dispute Settlement (ISDS) mechanism contained in its Chapter Nine. With Massachusetts Senator Elizabeth Warren leading the charge in this new fight, and a recent letter circulated to members of Congress by more than two hundred economists and law professors bolstering Senator Warren's opposition, the TPP's fate now seems intertwined with that of its ISDS provisions. The 7 September 2016 letter alleges that the TPP's ISDS "system undermines the important roles of our domestic and democratic institutions, threatens domestic sovereignty, and weakens the rule of law."[1)]

These critiques consist of alarming general statements that in many cases are not supported by the letter of the TPP. For instance, the 7 September 2016 letter states that "essentially, corporations and investors use ISDS to challenge government policies, actions, or decisions that they allege reduce the value of their investments."[2)]. But this description omits a fundamental premise of ISDS, which is that policies or regulations may only be challenged if they violate the relevant treaty. The reduction in value of an investment, in and of itself, is insufficient to challenge a government policy or regulation, and this is made plain through even a cursory reading of the TPP.[3)]. Likewise, critics claim that Chapter Nine will allow investors to bring claims against States "for actions that allegedly violate loosely defined investor rights to seek damages"[4)], but they omit that the TPP has made large strides towards clarifying the contours of key substantive protections.

These critics also misrepresent the fundamental motivation for the United States to negotiate and accept an investment chapter in the TPP, which is to protect American investors abroad. Indeed, few foreign corporations would hesitate to invest in the US out of a lack of confidence in its domestic courts. On the contrary, many American investors seeking to expand into developing markets will carefully assess the legal protections in place before investing abroad. By providing these American investors with the protection needed to securely invest, ISDS is mostly beneficial to them.

There is no doubt that ISDS can be improved. Criticisms of the system are not new, and have been stumbling blocks in the negotiation of other investment treaties, such as the TTIP. Nevertheless, the solution is not to abandon the system, but rather to address *valid* criticisms in order to improve it. This has been the case in the context of the TTIP negotiations, where the European Commission

has proposed the creation of the so-called investment court to address concerns regarding arbitrators' impartiality and the system's transparency. Although it does not contain such an institutionalized solution, the TPP does not rule out the possibility of adopting some of the measures proposed in the context of the TTIP negotiations[5], and proposes other innovations that are intended to improve ISDS.

In light of the criticisms of the investment provisions of the TPP, it is worth taking a closer look at its Chapter Nine. We will do so through the lens of three major concerns put forward by critics, namely, the supposedly undemocratic nature of the TPP's ISDS system, its impact on State sovereignty and the transparency of the system.

Part I of this blog post will deal with the supposedly undemocratic nature of the TPP's ISDS system, and **Part II** with the two remaining criticisms.

Democratic and Public Interest Aspects

Much of the criticism of the TPP's ISDS system focuses on its allegedly undemocratic nature. In a nutshell, it is said that ISDS allows investors to bypass US law and the US Court system, granting "corporate lawyers" the power to rule on investment claims that expose TPP parties, such as the US, to huge liability[6].

Allowing "corporate lawyers" to rule on claims against the US

According to critics, ISDS is fundamentally flawed because of an inherent bias among arbitrators towards investors. Senator Warren argues that, under ISDS "highly paid **corporate lawyers** would go back and forth between representing corporations one day and sitting in judgment the next … if you're a lawyer looking to maintain or attract high-paying corporate clients, how likely are you to rule against those corporations when it's your turn in the judge's seat?"

Although, undeniably, more work can and *should* be done to reinforce the independence and impartiality of arbitrators, Senator Warren's criticism should be read in light of the available information in order to avoid blowing the issue out of proportion.

First, if we were to assume that this bias exists, States would have lost most of their investment disputes. Statistics from UNCTAD reveal that this is not the case. In 2015, States obtained a favorable outcome in 47% of cases, including cases in which investors' claims were dismissed or dropped, and decisions that awarded no damages. On the other hand, investors were outright victorious in only 27% of cases, and obtained a settlement in another 26%[7].

Second, under any given set of arbitration rules, a respondent State has the right to appoint one arbitrator, and the chair of the tribunal is determined by the party-appointed arbitrators. Furthermore, under ICSID rules, when there is no agreement on the appointment of the chair of the tribunal, he or she will be selected by the Chairman of the Administrative Council from a list made up of arbitrators chosen entirely by States[8]. States are, thus, highly involved in the designation of the arbitrators that will decide their disputes.

Third, the TPP is the first ever treaty to provide for a Code of Conduct. If well structured, this Code could serve to dispel concerns about "no oversight or accountability of the private lawyers who serve as arbitrators …"[9].

Exposing the US to huge liability

Critics also allege that "ISDS would allow foreign companies to challenge U.S. laws – and potentially to pick up huge payouts from taxpayers – without ever stepping foot in a U.S. court."[10]. This criticism lacks supporting evidence. According to the US Trade Representative, the US currently has a total of 50 ISDS agreements in force, yet only 18 cases have been brought against it by foreign investors and not a single one has so far led to a finding against the US.

One must bear in mind that foreign corporations looking to expand their business in the US have little incentive to undertake highly public litigation against the government of the world's largest economy.

Bypassing US law and US courts

Critics often say that ISDS would free investors "from the fundamental rules of domestic procedural and substantive law that would have otherwise governed their lawsuits against the government."[11].

This criticism reveals a lack of understanding of the rationale behind ISDS. ISDS tribunals exist to serve as neutral forums for disputes that cross borders and that often involve delicate international law questions that may relate, for instance, to discrimination against foreign investors and investments. In addition, foreign investors enjoy distinct rights under international law. An ISDS panel composed of lawyers specialized in international law is better suited to decide these disputes, where international law – and its interpretative principles – are applied.

In any case, it is untrue that local laws or court decisions are left aside under ISDS.

First, while disputes under Section A of the Chapter Nine shall be decided in accordance with the treaty and applicable rules of international law, this is "without prejudice to any consideration of the domestic law of the respondent when it is relevant to the claim as a matter of fact"[12].

Second, when a tribunal is called upon to interpret an investment agreement or authorization, it shall do so in accordance with the applicable law, which will almost always be the law of an American jurisdiction[13].

Third, arbitrators routinely rely on decisions from local courts – especially supreme or constitutional courts – when construing and applying the domestic law of various jurisdictions.[14]

Continue to **Part II**.

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References

?1 Laurence Tribe et al., “220+ Law and Economics Professors urge Congress to reject the TPP and other prospective deals that include Investor-State Dispute Settlement (ISDS)”, 7 September 2016, p. 2

?2 Id., p.1

?3 See Article 9.6, para. 4, of the TPP

?4 Laurence Tribe et al., id., p. 1.

?5 Article 9.23(11) of the TPP provides that, in case an appellate mechanism is developed, TPP parties “shall consider whether awards rendered under Article 9.29 (Awards) should be subject to that appellate mechanism”

?6 Laurence Tribe et al., p. 3

?7 UNCTAD, World Investment Report 2016, p. 107

?8 Article 13(1) of the ICSID Convention

?9 Laurence Tribe et al, id., p. 3

?10 Elizabeth Warren, id.

?11 Laurence Tribe et al., id., p. 2

?12 TPP, Article 9.5, para. 1, footnote 34

?13 Id., Article 9.25.2

?14 See Gami Investments, Inc. v. Mexico, Award, 15 November 2004, para. 41: “It was for the Mexican courts to rule on the licitness of the expropriation as a matter of Mexican law. The present Tribunal defers to the Sentencia as an authoritative expression of national law.”