Kluwer Arbitration Blog

2021 in Review: From Fragmentation to Harmonization through Investment Treaty Arbitration (ITA) Reform

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The year 2021 has been perhaps the most controversial year for investment arbitration. From the profound structural reform work with respect to the ICSID and UNCITRAL rules, through the complete ban and termination of intra-EU investment arbitration in the European Union, to the ECT modernization process, this year has been marked by change and reform of the institutions, treaties, and procedural rules that make-up a large part of investment arbitration. This post will examine the most important structural reforms in ITA to consider how they aim to overcome the legal fragmentation of ITA and address the concerns of all stakeholders involved in investment arbitration.

ECT Modernization

In 2021, the fourth (2–5 March), fifth (1–4 June), sixth (6–9 July), seventh (September 28–October 1), eighth (9–12 November), and ninth (December 13) ECT modernization rounds were finalized. Despite the ongoing efforts to address the list of modernization topics approved by the ECT Secretariat in 2018, there are still difficult discussions that have yet to be resolved in light of the recent modernization rounds.

In 2020, the Blog ran a series on the ECT modernization process, followed by an update post in 2021. The modernization process will address both substantive and procedural aspects of ITA under the ECT. As discussed by Dr. Esmé Shirlow and Ylli Dautaj in the update post, the ECT modernization process may be moving closer to protecting "green investments"(and, leaving out the protection of fossil fuels), by redefining the terms *"Energy Materials and Products"* and *"Economic Activity in the Energy Sector."* Similarly, one of the critical objectives of the reform is to balance the interests of investment protection with environmental goals, taking into consideration the EU's goal to make the ECT the *"greenest investment treaty of all."*

The ECT modernization process has also touched upon valuation of damages in ITA. In the absence of clear guidelines to assess damages under the Charter, this task has been left to the tribunals. The ambiguity of the *"express compensation standard"* in article 13 of the ECT fails to provide sufficient guidance on compensation and valuation. Thus, the modernization process must provide a comprehensive compensation standard to overcome this issue (see here).

In the latest meeting, among others, the Modernization Group debated the *"Fair and Equitable Treatment (FET)"* standard based on a new text proposal. As previously argued on this blog, the protection offered to investors is, yet again, ambiguous: the FET standard may be no more than a reference to the minimum standard of treatment under customary international law.

The ECT Modernization Process and the EU: An Alternative to an ITA Ban?

Within the ECT modernization process, the EU has affirmed its support for modernizing the ECT according to its agenda by creating a multilateral investment court for future investment disputes in Europe (see here). Similarly, the European Commission has highlighted that it will closely monitor the ECT modernization process to ensure that the reform aligns with core EU values, including fulfilling the Paris Agreement commitments, even considering withdrawal if necessary.

In parallel with the modernization of the ECT, the EU has also pursued broader systemic reforms. These reforms have been underpinned by several judgments of the CJEU, including the September 2, 2021 ruling in *Komstroy v. Moldova*. In that decision, the CJEU held that ECT intra-EU arbitrations are contrary to EU law. This decision was built on the *Achmea* decision, where the CJEU found that intra-EU investment agreements and arbitration provisions are incompatible with EU law (here). Similarly, in the *PL Holdings* decision, the CJEU extended the reasoning in *Achmea* (covered here) and *Komstroy* (blogged here) to ad hoc arbitration agreements identical to arbitration clauses of intra-EU BITs (blogged here). These rulings have had a spillover effect on the ECT modernization process, shifting the negotiations paradigm and casting doubt on the future of ITA within the EU (see e.g., here); thus, reinforcing the EU's decision to terminate all intra-EU BITs. Despite the Termination Agreement initially not applying to ECT disputes, it shows the EU's efforts over the past decade to abolish intra-EU investment arbitration proceedings from the European legal order (see here).

UNCITRAL Working Group III Update

Since the Blog's series on UNCITRAL's Working Group III ("WGIII") in 2020, WGIII has held three sessions in Vienna, each covering big-ticket items on its agenda of possible reforms; namely, (i) selection and appointment of ITA tribunal members (ii) appellate mechanism and enforcement issues; and (iii) the draft Code of Conduct.

First, WGIII's discussions during its 40th session in February illuminated how adjudicators would be selected and appointed in an ITA standing mechanism, should it be implemented. For instance, due to the costs and complexity of a *"full representation body"*, preference was expressed for a selective representation model, whereby not all contracting States would be represented in the pool of adjudicators. In such cases where the respondent State was not represented in the standing body, WGIII has considered whether the respondent State could be involved in the appointment of *ad hoc* judges familiar with the State's domestic legal system, in a manner similar to that used in the ICJ, the International Tribunal for the Law of the Sea, and the European Court of Human Rights.

WGIII noted that the number of judges in the selective model should be based on the projected caseload and adjusted as the number of contracting States increased. The options for selection and appointment include: (i) direct appointment by each State; (ii) appointment by a vote of the

contracting States; or (iii) appointment by an independent commission. To avoid this process being politicized, it was suggested that it be multi-layered, open to stakeholders, and transparent. However, given WGIII is yet to make any decision on the desirability and feasibility of a standing body, such considerations remain open for further discussion at future sessions.

Second, during its 40th session, WGIII also considered the nature, scope and effect of an appellate mechanism. Recently, WGIII released its revised initial draft provisions, which identify the following grounds of appeal: an error in the application or interpretation of the law; manifest error of fact; an error in the assessment of damages; the tribunal lacked impartiality/independence or was improperly appointed/constituted; the tribunal wrongly accepted or denied jurisdiction; the tribunal ruled beyond the claims submitted to it; and a serious departure from a fundamental rule of procedure. Dr. Margie-Lys Jaime discussed the scope and standard of these grounds of review in-depth, contending that although:

> *"the appeal proceedings may entail additional time and costs (particularly if the tribunal is vested with the power of reviewing findings of fact), the appeal mechanism would substitute the annulment/set-aside proceedings, without adding an additional layer of control to the process."*

Indeed, WGIII appeared to favor this approach, including by requiring disputing parties to submit a waiver of judicial review, although, given the issues this would raise regarding the independence of domestic courts and the constitutionality of such a waiver, it remains to be seen how this will be achieved.

Thirdly, during the 41st session in November, WGIII discussed the means of implementing and enforcing the Code of Conduct, the second version of which was released earlier this year. The Code is intended to provide a uniform approach to requirements applicable to adjudicators vis-à-vis independence and impartiality. This issue was reignited following the annulment of the *Eiser v. Spain* award in 2020, in which the claimant-appointed arbitrator omitted to disclose a professional relationship with the claimants' damages expert (see, here). The delegates at WGIII have indicated that further sanctions for such non-disclosures could be written into the Code as a deterrent, such as reduced remuneration and disciplinary measures. As Professor Chiara Giorgetti previously summarized, the enforcement measures that are ultimately agreed upon by Member States will be *"key to the success of the Code."* This enforcement issue continues to be debated, and will largely depend on how the Code is implemented. Currently, the proposed implementation options include implementation through a multilateral instrument, on a treaty-by-treaty basis, by agreement on a case-by-case basis, or through the arbitral institutions themselves, by incorporating it in the procedural rules, adjudicators' declarations or court rules and regulations. Despite the need for a uniform approach, the Code's disclosure obligations are not without issue. Fahira Brodlija argues that *"[r]adically expanding disclosure obligations in the new Code would inevitably raise the expectations of the parties, resulting in an increase of challenges."* The Code has been further discussed here and here.

WGIII is scheduled to continue these discussions in February 2022 at its 42nd session to be held in New York.

Proposal for Amendment of the ICSID Rules

In 2021, the ICSID Secretariat published two working papers containing proposals for rule amendments: Working Paper 5 in June 2021 and Working Paper 6 on November 12, 2021. These papers build on the previous proposals, namely Working Papers 1, 2, 3, and 4, resulting from extensive consultation with stakeholders. WP6 marks the *"culmination of the five-year consultative process on updating the ICSID rules for arbitration, conciliation, and fact-finding"*. Adoption of these rules requires approval by two-thirds of Member States, and they are expected to be voted on (and adopted) in early 2022. While by no means exhaustive, below we highlight noteworthy features of the amended rules:

1. *Mandatory Disclosure of Third-Party Funding (TPF)*

In WP4, ICSID defined third-party funding as situations in which a party *'has received funds for the pursuit or defense of the proceeding through a donation or grant, or in return for remuneration dependent on the outcome of the proceeding'* (see, here). Similarly, WP5 settled the obligation to disclose TPF and the parties' obligation to disclose the name and address of any non-party from which they received funding, directly or indirectly. These disclosure obligations apply throughout the proceeding. In this vein, WP6 adds additional disclosure obligations for parties backed by TPF, including the obligation to disclose the names of the persons and entities that own and control a funder that is a juridical person. In case the tribunal needs to request additional TPF information, it can do so under rules14(4) and 36(3) of Arbitration Rules (AR).

2. *Greater Transparency for Proceedings*

Transparency has been a significant issue since the consultative process started. Greater transparency is linked to higher accountability of investment tribunals and greater support from civil society. In this regard, the proposed rules have tried to increase transparency through increased publication of awards, decisions, and orders. The current ICSID Rules require consent from both parties to publish the outcome award. The proposed wording of the new Arbitration AR 62 and new Additional Facility Rule 73 would stipulate that absent a clear objection in 60 days, a party will be deemed to have consented to the publication of the award. Orders and decisions would be published according to the same parameters under AR 63 and AFR 73.

The ITA reforms discussed above showcase the efforts of the arbitration community to address stakeholders' concerns as to the need for transparency, participation and accountability in investment arbitration. These structural reforms, and their relationship with the legal fragmentation of ITA, will be discussed in more detail in our upcoming series on the Blog: Regime Interaction in Investment Arbitration.

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