Response: European Commission report on investment protection in TTIP

The debate over investment protection, and in particular the investor-state dispute settlement (ISDS) mechanism, in relation to the Transatlantic Trade and Investment Partnership (TTIP), has been plagued by misconceptions as to the scope and implications of this clause. The results of the Commission’s 2014 consultation on the topic reflect continuing misunderstandings about the consequences of ISDS in a number of different areas:

- **States’ right to regulate**: Contrary to popular perception, ISDS is strictly about compensating investors for unexpected and arbitrary action by governments. Governments remain free to regulate, expropriate and ban in line with domestic and EU law.

- **A pro-investor bias by arbitrators**: Arbitral tribunals ruling on investor-state disputes are agreed to by both parties to ensure a fair ruling. This is reflected in the outcome of arbitration procedures, with 50 percent of concluded arbitration cases against EU Member States won by the Member State concerned, and another 26 percent settled.\(^1\)

- **The extent of frivolous cases**: The vast majority of disputes arise from policy changes by governments that endanger the capital and expected returns of established foreign investors. Heavily regulated sectors like agriculture, utilities and real estate are particularly affected, and claims typically concern the revocation of licences, the termination of contracts and/or fundamental changes to energy, healthcare and public-procurement markets.

The Commission has identified four areas for further improvement over the next quarter. In the following discussion each of the four is briefly addressed and some of the potential challenges and pitfalls are noted:

1) **The protection of the right to regulate**

In previous agreements containing an investment protection clause, governments have always retained the ability to regulate as per their own laws. However, the Commission has signalled its intention to include more explicit language as to the preservation of Member States’ right to regulate in the investment chapter in TTIP, particularly with regard to environmental, health and labour regulations.

The Commission should avoid creating uncertainty for investors as to whether or not they will be able to seek compensation in the face of unexpected government action. It is evident that no regulatory environment is permanent and that investors should be prepared for potential policy changes, yet providing adequate avenues for dispute settlement and sufficient compensation is essential. Moreover, the Commission should not try to address public perceptions of a pro-investor bias in ISDS by watering down investment protection to the point where it becomes ineffective.

2) **The supervision and functioning of arbitral tribunals**

In line with the ISDS clause contained in the Comprehensive Economic and Trade Agreement (CETA), the Commission seeks to include in the deal specific requirements of ethical conduct on the part of arbitrators, as well as a ‘roster’ of qualified potential arbitrators to ensure they have been previously vetted by the EU and the US.

The Commission should aim to preserve and strengthen the independence of ISDS arbitral tribunals. The roster would be agreed by EU and US officials in advance, and respondent states would have the ability to choose one arbitrator and vet the third one, as would investors. However, given the governments’ prerogative in selecting the roster, the Commission must avoid leaving investors vulnerable or creating the perception that the odds are stacked against them.

3) **The relationship between ISDS arbitration and domestic remedies**

The Commission favours the use of domestic courts to settle disputes between governments and foreign investors. It also seeks to prevent double litigation at international and domestic levels and over-compensation by ISDS tribunals.

It is important to preserve the ability of foreign investors to bring a case before an independent arbitral tribunal. If the seeking of redress is limited to domestic courts or if investors are required to exhaust local remedies before they can call upon ISDS tribunals, as has been suggested by some respondents to the consultation, the risk premium on foreign investment in the EU will be raised, while the cost and duration of legal proceedings (for both governments and investors) increases.

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The review of ISDS decisions for legal correctness through an appellate mechanism

The Commission aims to introduce a bilateral appellate mechanism of ISDS rulings that will review awards and correct potential errors. The goal is to ensure consistency in the interpretation of the investment protection clause in TTIP, and to provide an additional check on arbitrators.

Given that the Commission already aims to pre-select arbitrators via its roster, it seems that this mechanism would add a new layer of complexity and uncertainty into investment disputes, raising costs for all parties involved. It would appear that the goals of arbitrator consistency, accuracy and fairness would be sufficiently achieved through the roster.