BIAC Submission to the Public Consultation of the OECD on Investor-State Dispute Settlement

31 July 2012

Following the invitation by the OECD Secretariat to contribute to the Freedom of Investment Roundtable’s discussions on Investor-State Dispute Settlement (ISDS), the Business and Industry Advisory Committee to the OECD (BIAC) is pleased to submit the following comments on the issues and questions in the scoping paper as well as on other ISDS issues of interest (see Annex).

General Comments

1. The OECD Secretariat’s scoping paper is a valuable contribution to the very important issue of ISDS. We realize that the OECD’s efforts on ISDS are ongoing and that not every element of that work stream can be included or rehearsed in each paper in the overall effort. However, we suggest that such an important document like this scoping paper should not omit important background elements of the overall issue.

2. We would thus like to suggest to start the paper with key background, context, and bigger picture aspects of ISDS, e.g. the history of ISDS, how it came to be a core element in most significant Bilateral Investment Treaties (BITs) or comparable agreements, why a wide range of countries have come to see ISDS as so important, historic experiences/problems of both foreign investors as well as both host and home governments in dealing with investment disputes in the absence of ISDS etc. It would be helpful to lay out the importance of private sector-FDI in driving economic development, employment, competitiveness and growth. This very important basis and context could be addressed in the paper before giving details on specific provisions of ISDS. We also think it is important that a major paper like this addresses directly or by reference, macro- and micro-economic data about the impact of ISDS provisions on FDI flows.

3. For all countries, but especially for developing and transition economies, FDI flows are major determinants of economic performance. FDI transfers advanced technologies to non-OECD countries, which ensure their sustainable development. Hence, almost all countries assign a high priority to attracting FDI. Advanced industrial countries (including most OECD member countries) generally have a competitive advantage in attracting FDI for many reasons. But political and economic stability, rule-of-law, and predictable regulatory and judicial infrastructure are key elements in international investment decisions. It can be hard for developing and transition economies without a long and strong track record of rule-of-law, judicial independence, and public integrity to compete
to attract FDI. Investment treaties and international agreements, especially those including strong ISDS provisions, can play a key role in economic development strategies for many developing countries but implementation of some BIT commitments may remain problematic in the eyes of some foreign investors.

4. BIAC is aware of the need to balance the public good of an open investment climate and the public good of policy freedom. An important policy question in this respect is whether BITs limit in practice the policy space of host countries. This is contended by certain groups, but sufficient proof of the phenomenon is not provided. Independent research by the OECD on this issue may provide the basis for future policy work in this field. In this respect, it should be recalled that ISDS is not a substantive obligation, it is a procedural one. Therefore, ISDS in no way infringes the policy freedom of a government; it simply outlines the process by which a dispute over the underlining substantive principles in the investment agreement will be arbitrated. From a private sector perspective, the core investment protections and ISDS found in virtually all treaties is about ensuring the rule of law and baseline protections that all individuals and enterprises should be accorded and do not fundamentally challenge valid government regulation.

5. BIAC believes that independent arbitration is fundamental to investment protection. Without independent ISDS for foreign direct investment (e.g. arbitration in BITs) investment in non-OECD countries could be reduced for the simple reason that a foreign investor, uncertain of the local judicial regime, might be unwilling to make an investment. Access to a third-party neutral arbitrator reduces this perceived risk. There are various developments that favour local dispute settlement over international arbitration. The OECD paper should not be used as an argument to diminish international arbitration in investment matters.

6. The critical point for BIAC and the international business community broadly is that ISDS is an essential element in major international investment decisions. In today’s (and even more so, tomorrow’s) rapidly-changing and highly competitive global environment, international companies are prepared to deploy great sums of capital in pursuit of international investment opportunities. This is good for global economic growth, efficiency, economic development and overall global economic welfare. But as the volumes of money involved, and the competitive pressures rise, so does risk. Investors need to mitigate those growing risks if potential FDI flows are to be realized. For countries, particularly non-OECD countries, without strong long-established and independent judicial systems, strong ISDS provisions are critical. As well, ISDS provisions are widely viewed by the private sector as a critical backstop in all countries, especially when investors are considering major outlays of capital, long-term and complex projects, and projects involving government participation and/or participation of investors from multiple countries. ISDS provides businesses with a better leverage for proper discussions with host governments to resolve problems. Without ISDS, investors have no resort to protect global investment and business activities from unreasonable exercise of states’ authority.

7. Most FDI projects develop into very successful win-win efforts for all relevant parties, the host and home governments, the investor, and it new local partners and suppliers. But
unfortunately, too often, well-designed investment projects with strong economic fundamentals run aground on one of more political developments – e.g. expropriation (whether explicit, creeping, or by intimidation/harassment); change in the host government leading to unilateral re-writing of rules, regulations or contracts; imposition of onerous new forced localization dictates; failure to honor commitments on repatriation of the investor’s capital and operating funds; or other forms of harassment. Investment capital fears and flees risk, especially risk which cannot be mitigated. The substantive guarantees of investment treaties combined with ISDS offer a proven tool for relatively riskier countries to reduce their risk profile and thus be more competitive in the global race to attract scarce FDI.

8. The scoping paper includes several references and comparisons among international agreements on trade, human rights, multilateral environmental agreements, and investment agreements. Each of these areas and each of these sorts of agreements is very important. But we believe that trying to compare specific legal coverage and provisions, including dispute settlement provisions, in investment agreements with human rights or trade agreements is comparing apples and oranges under a broad category of fruit. In this context, we would like to note one fundamental difference between trade and investment. Trade is certainly closer to investment as an issue than is human rights or environmental protection. When trading, exporting and importing, the parties involved continue to reside and to conduct their business in their home countries, subject to the legal jurisdiction and protections of their home government. Only the goods or services trades cross borders into the partner country with the cross-border payment often assured or insured up-front. Thus, risk to the exporter or importer is quite limited. Although another form of conducting international commerce, investment or FDI is very different from trade. An investor takes large amounts of capital (money but also often skilled labor, intellectual property, trade secrets, etc.), and moves that capital to a foreign country, a long-term commitment (with all the commensurate risk) to operate under the jurisdiction of another sovereign government. Investment is fundamentally different from trade as investors put significantly more at risk, including the fundamental risk of being subject to a foreign government’s legal and regulatory system. Investors have much greater need of strong ISDS protections than traders in their home jurisdictions.

Specific Comments

1. Page 10, Chapter I.B. and Page 15, I.D.: BIAC does not see the added value of referring to other bodies of international law, such as Multilateral Environmental Agreements for this paper, especially as those agreements generally do not include provisions for investor-state dispute settlement. Such comparisons can provide interesting intellectual discussions, but their relevance is quite limited.

2. Page 15, I.D., Question 4: On balance, ISDS helps over time improve the domestic judicial and regulatory regimes of some nations, those that are and remain serious about attracting FDI. ISDS by itself is not going to deliver transparency, good governance, and rule-of-law if a government is not prepared to do the hard work to establish and enforce
those values. But it can help if the parties to an investment agreement share real commitments to those values.

3. Page 24, Chapter II.B., Questions 6-8: Cost is obviously a concern in ISDS as in any other area. But implying that, somehow, high costs alone might make strong ISDS provisions unaffordable is not correct and therefore should not be a reason to avoid or weaken ISDS protections. Fees may be high, but the stakes are high as well. It has to be realized that the economic consequences and damage involved can be very substantial. However, BIAC is open to the possibility of exploring best practices in bringing the cost of arbitration down.

The costs of ISDS should be put in perspective. The cost argument is often used by countries that are not in favour of independent ISDS and that seek to abandon arbitration. It should be realized that investment treaty arbitrations are often (technically) difficult. Material fees also ensure that companies will not enter into arbitration lightly. For the host state these fees should be an incentive to settle the matter as soon as possible. According to 2010 UNCITRAL rules the costs of arbitration should be borne by the unsuccessful party – “high” fees should be an incentive for efficiency.

It should be noted that in general only major cases are being arbitrated. Companies normally do not arbitrate on principle matters or when there are other forums and mechanisms that can adequately be used to prevent and resolve disputes. This could explain the figure of 8 million USD. Not all countries have a good track-record when it comes to respecting rights of foreign investors. If a state violates a treaty, it risks arbitration including the costs for such arbitration.

4. Page 26: ‘National systems’ cannot necessarily be a suitable alternative for ISDS as an independent judiciary is simply not available in every country. OECD countries should fully support independent arbitration as an alternative vehicle for enforcing host governments’ commitments and should not propose domestic systems for foreign investment dispute settlement as a substitute for ISDS. This could lead to non-OECD countries adopting the same approach. This will inevitably lead to a deterioration of the position of investors.

5. Page 27: National systems tend to focus on remedies that are non-pecuniary (e.g. annulling illegal action) and ISDS on pecuniary. BIAC does not see an issue here. An independent arbitrator could never force a government to annul or adopt a (legislative) measure. As a consequence, pecuniary sanctions are the only sanctions that could be awarded by an independent arbitrator. If a government, however, wishes to annul or revise a measure, it could always do so.

6. Page 36, Chapter II.D., Questions 12-16: Our members are increasingly concerned with the problems (real as well as potential) of enforcement of ISDS awards. While enforcement can be a problem in either direction, we are primarily concerned about the threat of increasing signs of some governments criticizing or even unilaterally annulling investment agreements and ISDS, invoking misguided concepts of sovereignty without any respect for legal obligations and commitments. Recent actions of the Government of
Ecuador, for example, in ignoring clear injunctions from international arbitrators are very troubling and should not be tolerated or ignored.

7. Page 58, Questions 29-34: “Forum Shopping” under competing arbitral bodies is a rather unfortunate description of an investor being able to take advantage of specific commitments in an agreement reached voluntarily between the two relevant governments, given the wide range of potential claims which could emerge years later under various scenarios. The implication that an aggrieved investor is somehow gaming the system or doing something improper is unjustified.

8. Page 62, Questions 35-41: “Consistency” is an important virtue, but it should not become a straight-jacket. As in domestic judicial and arbitral systems, the role of the arbitrator or judicial authority is to consistently apply the laws and regulations to a wide range of specific and quite different cases and situations. Consistency is important but does not trump other important criteria, most importantly adjudicating the case fairly. Justice and fairness are higher criteria than consistency.

9. Page 66, Section III.C., Questions 42-46: BITs cannot work without a strong and effective independent arbitration/dispute settlement. There could be issues with arbitration (costs, enforcement etc.), but it is the only system that guarantees impartial dispute settlement. Losing independent dispute settlement would, in practice, mean losing investment protection which would reduce much-needed FDI flows globally and especially flows into developing and transition economies.

As explained above, ISDS serves the interests of both the investor and the host country. The host country wants to attract FDI and sees ISDS and a key element in its investment climate package, a way to compensate and offer some protections for perceived issues in their investment regime or governance package. For the investor, the ability to access ISDS affords promise of a fair, unbiased resolution for disputes outside the potential control of the host government which could be a party, directly or indirectly in such disputes. It is normal, as in trade agreements or other fields, for model texts to evolve over time and/or to be customized to address specific issues with particular negotiating parties.
Annex 1

OECD Investor State Dispute Settlement Public Consultation

Submission from Business New Zealand

Thank you for giving Business New Zealand the opportunity to comment on the draft prepared by the OECD Secretariat.

Who are we?

Encompassing four regional business organisations (Employers’ & Manufacturers’ Association (Northern), Employers’ Chamber of Commerce Central, Canterbury Employers’ Chamber of Commerce, and the Otago-Southland Employers’ Association), BusinessNZ is New Zealand’s largest business advocacy body. Together with its 80 strong Major Companies Group, and the 70-member Affiliated Industries Group (AIG), which comprises most of New Zealand’s national industry associations, BusinessNZ is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

In addition to advocacy on behalf of enterprise, BusinessNZ contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.

BusinessNZ’s key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD (a high comparative OECD growth ranking is the most robust indicator of a country’s ability to deliver quality health, education, superannuation and other social services). It is widely acknowledged that consistent, sustainable growth well in excess of 4% per capita per year would be required to achieve this goal in the medium term.

Answers to your questions:

Your paper asks 41 questions. Many of these are extremely detailed. Rather than answer these we make some general comments that address many of these issues.

New Zealand is unusual for an OECD member. It is a net importer of capital. The interests of many of our members is therefore to encourage foreign investment into New Zealand rather than to protect foreign investments made offshore. That said many of our members do invest offshore and from time to time do experience government imposed difficulties with these investments. We are not sure what impact the negotiation of investment treaties containing ISDS has on the decisions of overseas investors in New Zealand. Australia has for many years been the major foreign
investor in New Zealand yet, it was only in 2011 that an investment agreement was negotiated between Australia and New Zealand.

New Zealand is by many measures seen as the world’s least corrupt country. We also have an excellent legal system. Foreign investors know that if seeking recourse to our system they will receive an impartial hearing and equal treatment to local investors. We suspect that this is a much more important factor for investors in New Zealand than ISDS in treaty arrangements.

New Zealand investors offshore are not always investing in economies that have good functioning, un-biased domestic dispute settlement arrangement and policy-making processes. This is why New Zealand has encouraged the negotiation of treaties including ISDS with such countries.

Business New Zealand welcomes the negotiation of treaties containing ISDS with countries of this type. It sees no compelling need to negotiate treaties containing ISDS with countries of similar type to New Zealand.

ISDS has been a controversial issue in New Zealand over the past 13 years or so. The controversy began with the negotiation of the Multilateral Agreement on Investment and has continued since then. It has become particularly controversial with the current negotiation of the Trans Pacific Partnership set against the backdrop of the ISDS cases involving Australia and decisions on the plain packaging of tobacco products. These cases have been very well publicized in New Zealand. With strong pressure coming on the New Zealand Government to follow a similar path to Australia on tobacco, there is concern that ISDS could be used against New Zealand. (Those arguing along these lines conveniently forget that New Zealand’s investment agreements allow the Government to regulate for reasons such as protecting public health).

It is unfortunate that Australia is being challenged by companies using two of its Treaty agreements with jurisdictions where the companies are obviously not domiciled. This Treaty gaming does have unfortunate consequences as it plays into the hands of the vocal critics of Investor State Dispute Settlement.

Our membership has no issues with the fees being charged by those representing parties in ISDS cases, nor are there strong views on experts playing different roles in different cases.

Our membership does have views on the different outcomes that are achievable from ISDS from remedies that would be achievable in domestic law. Large monetary settlements would be unlikely in New Zealand domestic law, but could be achievable through recourse to ISDS. A debate on this matter in the OECD context would be welcome. Some of our members do see a case for bringing New Zealand’s property rights protection in line with international law.

Thank you again for the opportunity to submit on these important matters.

Catherine Beard, Executive Director, ExportNZ and Manufacturing NZ, On behalf of BusinessNZ
Annex 2

OECD Investor State Dispute Settlement Public Consultation

Submission from Repsol S.A.

1. **Key issues** (para 26). We agree with the key issues identified but would add the issue of time and delay, i.e. how long it takes for a dispute to be resolved through ISDS. This is a major concern of claimant investors, and some respondent states as well. This issue is treated in the paper together with costs (see e.g. box 2). However the matter is of fundamental importance in light of increasing delays (with some cases lasting up to ten years) and thus deserves separate and more detailed treatment. The credibility of the system with investors and thus its capacity to help attract investment (which is the concern of the states) depends on a critical analysis of how to control time and cost. We agree with the paper (Box 2) that ICSID internal delays have been controlled (time to register; time to identify arbitrators etc.). However, this is only a small part of the delay factors with the greatest delays occurring as a result of cases being split unnecessarily into different phases (jurisdiction, merits, damages) and awards taking commonly one year or more to be issued. The alleged improvement in time from case initiation to conclusion in Box 2 we suspect is due to termination of some cases early due to successful jurisdictional objections which may distort the figure. Our experience is that cases are not being resolved more promptly.

2. **Arbitrator selection.** ICSID should consider following the ICC’s lead in commercial cases by requiring not only that all arbitrators confirm their availability to dispose of a particular case promptly (human nature will always cause them to say yes) but by disclosing the number of other pending cases as counsel and arbitrator and a statement that they will be in a position to (e.g.) issue an award within a maximum six month time delay following a post hearing brief.

3. **Arbitrator case management.** Linked to the above comment, the paper could address more specifically the different techniques that may be adopted for arbitrators to manage the case more efficiently to speed up the process and reduce costs (it is only referred to in passing, e.g. in para 35 and box 2). Case management techniques may include: fixing all deadlines (including hearing dates and dates for the issuing of interim decisions and final awards) at the first procedural meeting; ensuring a tight calendar that respects state sovereignty but also recognises that “justice delayed is justice denied”.

4. **Bifurcation and trifurcation.** There seems to be no mention of these matters in the paper. Yet they are of concern to users of the system particularly in relation to the time/cost issue. There should be some discussion in the paper as to when bifurcation (separation of jurisdictional and merits phases) and trifurcation (adding a separate third phase on damages) are advisable and how to prevent them adding to delay. Particularly, tribunals should refuse jurisdictional bifurcation unless the jurisdictional issues have a material chance of success based on existing case law. It can add from 12-18 months additional time to the resolution of a dispute when compared with a case which is not bifurcated.
With regard to the splitting of liability and damages, this should be the exception and raised by the Tribunal contemplating it at the first procedural hearing. If ordered, this early decision would avoid the unnecessary and expensive process of unnecessarily proving damages in a pure liability phase and thus permit faster deadlines. The splitting of liability and damages is often used now by tribunals after hearing both liability and damage issues and then deciding that damages are "too hard" without the assistance of a tribunal appointed expert in a second repetitious damages phase.

5. Tribunal appointed experts. In the same context, once the tribunal has reviewed the parties' pleadings and considers that there is an issue of such complexity that it may need an independent expert (usually a damages expert), such expert should be appointed (subject to comments from the parties) prior to the final hearing. There is a disturbing trend to appoint such experts many months after the close of the final hearing once the tribunal realises it does not feel comfortable reaching a reasoned decision on damages on its own. Due to the late appointment, the expert is unfamiliar with the issues and needs to be educated from zero which adds further time and cost.

6. Arbitrator remuneration linked to issuing of decisions and awards. One of the fundamental problems with the current system (particularly ICSID) is that arbitrators simply inform the Secretariat what their anticipated workload will be for the next six months and the Secretariat asks for advances from the parties accordingly. The advances are not linked to any milestones but simply to time worked. This is to be contrasted with the remuneration mechanism in the ICC where the arbitrators are only paid once specific milestones are reached with most of the remuneration only paid once the final award is issued. This provides a great incentive to the arbitrators to be efficient and issue an award as promptly as possible and could be adopted in the ICSID or other ISDS systems. It is noteworthy that, with this remuneration system, ICC awards are almost twice as fast as ICSID awards with issues that are often equally complex.

7. Formalise a role for ICSID and the World Bank with regard to payment and enforcement of awards (para 69). The non-payment of awards is a major challenge to the system. Although there are legal mechanisms for enforcement, identifying attachable assets can be a long and expensive process. ICSID and the World Bank should consider protecting their ISDS system by establishing a mechanism that would support voluntary payment. This could include a constant review of the payment record of a state in respect of an adverse award and regular meetings with state representatives of those states that have failed to pay voluntarily with formal information about the status of payment and progress towards payment being reported to all other Member States of the World Bank and on the ICSID website. The current system simply washes its hands of the award once issued.

8. Allocation of costs (paras 39-42). Following from the above, another form of penalty against recalcitrant non-complying states could be a more systematic allocation of costs against those states in all cases where the investor claimants were successful. At the moment, there is a high degree of deference to states with costs rarely being awarded against them even where states lose.
9. **Forum shopping/treaty shopping** (section II.G). This section addresses the possibility of structuring an investment to attract treaty protection. We suggest that the phrase "forum shopping" be replaced by a more neutral expression like "forum selection" or "treaty planning". This is a legitimate use of legal instruments.

10. **Annulment proceedings.** States are currently routinely using the annulment process in ICSID with unsustainable arguments just to obtain a stay of execution. To limit this abuse, any such stay should be conditioned on payment of security in the amount of the award. This used to be the case but is less and less frequent. If there is no "cost" to seeking annulment, states have a perverse incentive to using the remedy even where there are no chances of success.

11. **Consistency** (para 162 et seq.) It is a matter of concern that tribunals are reversing the consistent conclusions of a series of earlier cases leading to a lack of legal security. There should be a greater degree of restraint from later tribunals once an established line of case law has been established upon which investors may legitimately be assumed to have relied (similar to the restraint shown by domestic civil law courts in the respect for a jurisprudence constante). Whilst there is no strict doctrine of precedent, each tribunal should carefully consider and distinguish any earlier case dealing with similar issues rather than simply deciding from zero. Consistency will reduce litigation, give greater credibility to the system and maximise settlement opportunities. [This issue is close to our heart in light of the inconsistent case law on the 18 month litigation period before Argentine courts].

12. **Injunctive relief.** Although it is not expressly mentioned throughout the document, we feel that it would be extremely helpful for investors submitting claims to ICSID to regulate the possibility of requesting as cautionary measure the Court to order the stay of all legal proceedings initiated and existing under local law in relation to the matter under litigation, while the claim before ICSID is still pending.