Not a reason (and many risks) in sight: ISDS in the Transatlantic Trade and Investment Partnership (TTIP)

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Including investor-state dispute settlement (ISDS) provisions in TTIP, which is currently being negotiated between the US and the EU, is an objective of both EU and US negotiators. The ISDS-TTIP plan has provoked an outcry among civil society, in particular with the EU. In a letter addressed to the responsible trade officials in the US and the EU[1] about 200 civil society organizations from both sides of the Atlantic criticize that ISDS undermines democratic decision-making. What are we to make of this debate?

In order for a public policy measure to be adopted – and TTIP is such – the public welfare gains, framed in whatever terms, should outweigh the disadvantages. In order to preserve the necessary decision-making space also for the future, no responsible legislative body, neither in the US at federal and state level, nor in the EU at European and Member State level, should sign away the right of their elected successors to legislate in ways that express the collective preferences of the people they serve. It is in the nature of public-interest law-making that it must regulate and *in extremis* prohibit activities that produce a social, health or environmental harm or otherwise cause a nuisance to public interests, even and especially if they are profitable and thus self-perpetuating.

Let us therefore look first at the rationales provided for ISDS in TTIP and then at the potentials risks for the regulatory space in the EU and the US resulting from it:

The conventional rationale for ISDS is, of course, that it would foster foreign direct investment and thus economic welfare, providing a kind of insurance for investors against political risks and shortcomings in the legal and judicial system of the host state. Whether that economic rationale holds true at all is much debated in the economic literature. It is, in any instance, highly questionable in the relations between two developed rule-of-law legal systems like the ones of the EU Member States and the US. For example, a recent study by the London School of Economics[2] concludes that there is no convincing evidence that past US treaties with investment protection clauses have had a tangible impact on US outward investment, even in "risky jurisdictions". Another study[3] concludes that worries over deficiencies of the US judicial system are not “sufficiently substantiated” to warrant an inclusion of ISDS in TTIP. In the case of TTIP, the economic rationale for ISDS is hence simply and plainly unconvincing.

A second argument is that ISDS should be included in TTIP, because the EU would like to treat alike all its trade partners with whom it is currently negotiating trade and investments agreements - these include China and Japan. However, international politics and law are rarely guided by a rationale of treating every country equally. To give just two examples: Citizens from different countries are routinely treated differently in visa regulations. Many countries distinguish between different

[1] http://corporateeurope.org/sites/default/files/attachments/ttip_investment_letter_final.pdf

[2] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/260380/bis-13-1284-costs-and-benefits-of-an-eu-usa-investment-protection-treaty.pdf

[3] http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2410188

destination countries in arms control regulations – and rightly so. Has anyone ever worried about this being offensive to the disadvantaged countries like some now seem to do with regard to China being offended over being asked to sign ISDS provisions?

A slightly different version of this argument is that the two major economic powers should agree on a "gold standard" of ISDS, capable of being multilateralised later on, to remedy some of the existing shortcomings of the system. This argument is made against the failure of past attempts to deal with investment multilaterally such as the (rightly) long-dead MAI or the injection of investment issues in the WTO's Doha Round. Indeed, there seems to be wide agreement that ISDS as it currently mostly works suffers from some serious flaws – maybe also due to some mistakes made by governments in the past. A reform is indeed urgently needed. However, does this mean that there should be a bilateral solution to what is essentially a multilateral problem? I do not think so. Some countries may even perceive that as a quite neo-imperial type of behaviour by two of the major economic powers.

If there is little, if anything at all, speaking in favor of ISDS in TTIP, what is on the negative side? As is well known, decisions by international arbitrations tribunals – as far as published in first place – are not a consistent body of law; this may be in part due to the absence of an appellate mechanism and is certainly due to the widely varying and vague formulations in international investment agreements. Thus, some of the case law could be read as involving interpretations of e.g. the fair and equitable treatment or clauses prohibiting indirect expropriation that might lead to situation where a state has to be compensate to the investor for certain regulatory measures, adopted e.g. for the protection of the environment. While it is difficult methodologically to prove in a large scale, comparative exercise that the mere threat of ISDS proceedings would lead states to not adopt regulatory measures or to resort to less stringent regulation, there is certainly anecdotic evidence for such "regulatory chill".

Arguably, phrasing substantive investment-related clauses narrowly and defining well central terms like "indirect expropriation" would remedy some of these shortcomings. This is indeed proposed by the EU Commission.

However, there is no rush and point at all for doing this now in TTIP. Instead, let us take some time to decide on the appropriate multilateral forum for such a venture. Let us then, building on existing work by UNCTAD and others, develop a model investment agreement that does not only define the rights of investors, but also their obligations in relation to the protection of the environment, their workers and human rights at large. Let us then thoroughly consider and assess, with a broad involvement of civil society, what are the appropriate judicial mechanisms for protecting all of these interests – including the ones of investors in concerning a rule-of-law treatment. And if at the end of that, there is a conclusion that ISDS is an appropriate mechanism for this purpose – let us get it right then.

This opinion piece is based on the following study, commissioned by the German Heinrich-Boell-Foundation and co-authored by Christiane Gerstetter and Nils Meyer-Ohlendorf, Ecologic Institute: http://www.boell.org/downloads/HBS-TTIP_2.pdf

The views in the above text are expressed by Christiane Gerstetter in her individual capacity.