European Commission Proposal for Permanent Investment Courts

December 2015

Background

On 16 September 2015 the EU Commission published a proposal that would see a system of permanent courts replacing arbitral tribunals as the method for Investor State Dispute Settlement (***ISDS***) in the Transatlantic Trade and Investment Partnership (***TTIP***) Agreement with the US. The proposal was finalised on 12 November 2015, apparently after consultations with the Council and the European Parliament, though neither of these bodies has formally approved it as yet. For its part, the US has not expressed agreement with the proposal.

The proposal takes its inspiration from adjudicatory models which operate between states (such as the WTO bodies) or are controlled by states (such as the Iran-US Claims Tribunal or "mixed commissions" of prior centuries). There is to be a Tribunal of First Instance composed of 15 judges (five EU nationals, five US nationals, and five nationals of third countries) and a six-member Appeal Tribunal (two EU nationals, two US nationals, and two nationals of third states). Cases will be heard "in divisions consisting of three Judges", or "a sole Judge who is a national of a third country" for relatively small cases.

The Commission's stated goal is to "replace the existing... ISDS mechanism in TTIP and in all ongoing and future EU trade and investment negotiations."[1] Note, however, that the Trans-Pacific Partnership (***TPP***) Agreement, whose text was released on 5 November 2015, relies on arbitration for ISDS. On the other hand, the EU-Vietnam Free Trade Agreement, signed on 2 December 2015, does refer to investment courts (the text is yet to be released). It remains to be seen how future negotiations for "Deep and Comprehensive Free Trade Areas" (DCFTAs) with Morocco, Tunisia, and Jordan will proceed.

EU Trade Commissioner Malmström has stated that the objective is to create an ISDS system which is "accountable, transparent and subject to democratic principles."[2] This note critically examines this claim.

The accountability argument

The judges of the proposed courts are to have "qualifications comparable to those found in national domestic courts, or in international courts such as the International Court of Justice or the WTO Appellate Body."[3]

Yet it has never been suggested that, on the whole, arbitrators sitting in investment disputes lack the necessary expertise. Indeed, ICJ judges and WTO Appellate Body members, who would be eligible judges under the Commission proposal, are regularly appointed in investment arbitrations. In disputes requiring specialised knowledge of specific industries/sectors, it is likely that permanent judges will be less qualified than arbitrators specially selected for the particular case.

What is more, removal of party choice in the constitution of the panel seems to ignore that this is also a possible feature of permanent courts, such as ICJ and ITLOS Chambers.

[1] EU Commission, Press Release of 12 November 2015.

[2] C Malmström, "Proposing an Investment Court System" (Blog Post), 16 September 2015.

[3] Ibid.

Commissioner Malmström has stated that the proposed system will "guarantee there is no conflict of interest", apparently by ensuring that "you won't be able to choose which judges hear your case".[4] This claim seems to be problematic on two counts. First, if party appointment were inherently a source of conflicts of interest, that would raise doubts about commercial arbitration as well. Yet it is well established that party appointment is an essential feature of arbitration, itself embedded in national legal traditions.[5] Secondly, the Commission's proposal provides that persons who are government officials or receive an income from the government "but who are otherwise independent of the government" are eligible to be appointed as judges.[6] Yet such links of dependence from States would normally rule out the viability of an arbitral appointment.

Note also that while under the Commission's proposal only the President or a Sole Judge will be a third-country national, investment tribunals routinely comprise third-country nationals.

Finally, one may question the efficiency of creating a plethora of standing judicial office-holders whose function would be exclusively to serve in investment disputes which may never arise.

The transparency argument

Transparency *is* consistent with arbitration. Investment arbitrations under the auspices of ICSID, NAFTA and CAFTA-DR, or pursuant to the 2014 UNCITRAL Transparency Rules, offer more transparency than many domestic judicial proceedings, or indeed WTO procedures. As for *amici curiae* briefs, these are more prevalent in investment arbitration than in any other international forum.

The democracy argument

Commissioner Malmström noted that "the Investment Court System will also enshrine governments' right to regulate", including "a direct instruction to the judges, which the appeal will ensure is properly respected." But the regulatory latitude that States enjoy is a matter of substantive law. NAFTA Commissions in particular have issued binding interpretations of the applicable provisions, which arbitral tribunals are bound to observe.

Consistency with the ICSID Convention

The Commission's proposal provides for arbitration under (*inter alia*) the ICSID Rules,[7] stipulating that consent to bring a case before the proposed courts "shall be deemed to satisfy the requirements" of Article 25 of the ICSID Convention[8] and that the ICSID Secretariat may serve these courts.[9] Yet it is unclear whether the proposal is compatible with the ICSID Convention.

Modification of a multilateral treaty as between certain of its State Parties ("inter se modification") is allowed only if expressly provided for by the relevant treaty, or if substantively compatible with the treaty's object and purpose.[10] The ICSID Convention does not provide for inter se modification agreements, nor has any such agreement been tested.

The Commission proposal raises three key concerns:

- Arbitration, including an entitlement to appoint an arbitrator, is the main object of the ICSID Convention.

[4] Ibid.

[5] See, eg, Regent Company v Ukraine (ECtHR, 2008, para 54); Lithgow v UK (ECtHR, 1986, para 201).

[6] Section 3, Article 11(1) of the Commission's November 2015 proposal for the Investment Chapter of TTIP.

[7] Id, Article 6(2)(a).

[8] Id, Article 7(2)(a).

[9] Id, Articles 9(16) and 10(15).

[10] See Article 41 of the Vienna Convention on the Law of Treaties (1969), which codifies the ICJ Advisory Opinion in Reservations to the Convention on Genocide (1951).

- A number of the main functions of ICSID under the Convention appear incompatible with standing courts. This is the case notably for ICSID's screening of Requests for Arbitration, its role in constituting arbitral panels, and its handling of challenges to arbitrators.

- The remedy of annulment is central to the ICSID system. But ICSID *ad hoc* Committees would be replaced by the proposed Appeal Tribunal, which would enjoy considerably broader powers of review, including for "manifest[] err[or] in the appreciation of the facts, including the appreciation of relevant domestic law".[11]

None of these concerns were present in an earlier idea for an *optional* ICSID Appeals Facility that would see appellate formations empanelled from among 15 arbitrators selected by ICSID. That idea was discussed in a 2004 paper by ICSID,[12] and was ultimately not pursued because it was thought to be "premature", "particularly in view of the difficult technical and policy issues".[13]

The Luxembourg Courts

The Luxembourg Courts clearly consider themselves as the ultimate arbiters of EU law issues, as was made plain in the *EPO* and *MOX Plant* cases. Given that the proposed investment courts are not to be subject to the CJEU's control, through preliminary rulings or otherwise, it is open to question how Luxembourg will react to the Commission proposal.

Is a regional approach viable?

The Commission proposal seems to be a transitional step towards the creation of an international investment court. That is of course an idea that has been mooted from the outset, notably in the proposed Abs-Shawcross Convention of 1959 that is a progenitor of modern-day BITs. The idea always stumbles upon the composition of such a court and the appointment of its members. It is difficult to side-step these difficulties by putting in place regional/bilateral standing courts. Indeed, ICSID recorded in 2005 that there was "general agreement that, if international appellate procedures were to be introduced for investment treaty arbitrations, then this might best be done through a single ICSID mechanism rather than by different mechanisms established under each treaty concerned".[14] And a 2013 UNCTAD study concluded that an international investment court – if at all viable given the thousands of bilateral and multilateral treaties now in place – would be "difficult to implement as it would require a complete overhaul of the current regime through a coordinated action by a large number of States".[15]

The legitimacy of investment protection and investment arbitration are questioned by a number of constituencies in Europe. Whether the concerns voiced will resonate with Europe's economic partners remains to be seen. Doubtless the serious questions of law and policy raised by the Commission proposal will be raised in the negotiations. They are yet to be given persuasive answers.

[11] See Section 3, Article 29 of the Commission's November 2015 proposal for the Investment Chapter of TTIP. Note that only the appellate decision would qualify as a final Award pursuant to the ICSID Convention.

[12] See "Possible Improvements of the Framework for ICSID Arbitration" (ICSID Secretariat Discussion Paper, October 2004).

[13] "Suggested Changes to the ICSID Rules and Regulations" (ICSID Secretariat Working Paper, May 2005) p4.

[14] Ibid.

[15] UNCTAD, "Reform of Investor-State Dispute Settlement: In Search of a Roadmap" (June 2013) p 9.