Your voice.
Your interests.
Your future.

RESPONSE TO CONSULTATION

Brussels, 11 July 2014
Answer to EC Consultation.06

CEEP RESPONSE TO THE EC CONSULTATION ON ISDS IN TTIP

Executive summary

- CEEP acknowledges the efforts made by the European Commission in identifying reasons for concerns and bringing some answers. More is however expected from the European Commission on some specific issues. **CEEP is ready to contribute to the Commission's** task by providing its expertise and our contribution to the EC Consultation on ISDS in TTIP is a first step done in that direction.

- CEEP pleads for **more transparency on the ISDS**. The transparency mainly depends on the composition of the arbitral tribunals. CEEP would positively assess the introduction of the United Nations rules on transparency into TTIP, provided arbitrators don't make extensive use of the exceptions clauses on holding of public hearing and on disclosure of information.

- CEEP would like a **more extensive use of the roster list of arbitrators**. The roster should be exclusive and the listed persons should fulfill strict conditions of experience, independence and impartiality in line with a real and binding code of conduct to be adopted along with current negotiations on investment protection chapters. In case a roster system is implemented, parties should be involved in the choice of the conciliators and arbitrators in order to guarantee a fair and transparent process.

- A **real appellate mechanism must be implemented**. Relevant provisions regarding the composition of the appellate body must be included. CEEP is convinced that the WTO Arbitral Body model, based on collegiality, could be employed in case of ISDS in TTIP.

- European policies are evolving as a reaction to new challenges and evolving expectations of citizens and businesses. Competent authorities (European, national, regional or local level) are expected to reflect these norms and wishes. CEEP proposes that the **right for states to regulate encompasses a far broader scope** than the "legitimate public policy objectives on the basis of the level of protection that they deem appropriate". Such a provision should be extended to the general chapters on investment.

- CEEP also expects **additional clarification on the definition of "investment"**. That definition should only cover the capital employed and a reasonable equity yield rate, excluding expressly all kinds of future returns on the investment.

- The Commission and Member States must also consider the **inclusion of exceptions or carve-outs, such as prudential, essential security and taxation carve-outs**. This would help to achieve a proper balance between investor's protection and government's right to regulate by enhancing the host state's policy space.

CEEP GENERAL SECRETARIAT Rue des Deux Eglises, 26 bt 5, BE – 1000 Brussels
T: + 32 (0) 2 219 27 98 | F: + 32 (0) 2 218 12 13 | E: ceep@ceep.eu | www.ceep.eu
Registered stakeholder
ID Nr 59513031434-92

Question 1: Scope of the substantive investment protection provisions

The CETA text defines investment as "every kind of asset." The CETA text also provides an indicative list of such assets that can qualify as investment, covering enterprises, equity, bonds and debt instruments, intellectual property rights and others—independent of whether or not they are associated with an existing enterprise in the host state.

CEEP sees the open-ended list as problematic because it introduces elements of vagueness and allows for the most expansive interpretation by tribunals of what that definition encompasses, since the list that follows is merely indicative. This definition is therefore the least suitable for host states. CEEP believes that the scope of the substantive investment protection provisions increases the risks of being sued for states. For instance, in the field of fracking (shale gas) it is unclear if a moratorium (state decision) could lead to claims at the arbitral tribunal.

In this respect, CEEP proposes that:

- The notion "concession" should be restricted to permits for extraction or exploitation of natural resources.
- The definition of "investment" should only cover the capital employed and a reasonable equity yield rate, excluding expressly all kinds of future returns on the investment.
- The Commission and Member States consider the inclusion of exceptions or carve-outs, such as prudential, essential security and taxation carve-outs. This would help to achieve a proper balance between investor's protection and government's right to regulate by enhancing the host state's policy space.

Question 2: Non-discriminatory treatment for investors

On the basis of the "Most favoured nation" (MFN) clause, arbitrators now routinely allow investors to essentially cherry-pick provisions from other investment treaties that are more favourable to it. As a consequence, this clause alone is sufficient to undermine all of the objectives the European Commission states that it seeks in its approach.

To be more precise, it is not clear in the CETA text whether the non-discrimination clause of the investment chapter only covers investors which have already made an investment or also investors which plan to do so.

In addition, the Commission explains, that "*exceptions allowing the Parties to take measures relating to the protection of health, the environment, consumers etc. (...)*" should "*allow differences in treatment between investors and investments where necessary to achieve public policy objectives.*" Until now, public services have been subject to specific treatment and protective measures in many previous FTAs and in the GATS; due to their special nature they have benefitted from a positive list approach. Although the TTIP negotiations seem to favour the negative list approach, or at least the US does, a negative list approach would require all sectors that should not be included to be expressly referred to in the agreement, which would require that Member States actively campaign to the EC for exclusions in the agreement. Otherwise, all services are de facto within the scope.

CEEP favours a positive list approach and the same approach should be kept across the document in order to provide an adequately strong shield for public services. Potential consequences of other

approaches could be that public service markets could become, without public debates, subject to liberalisation. Naturally, this is not within the competence of the EU, but it should be up to the Member States to initiate such changes. Decisions and regulations in the field of public services (in particular protocol no 26 TFEU) and at the level of regional and local authorities (Article 4(2) TEU) should explicitly be excluded from the MFN.

CEEP suggests:

- To ensure that an MFN clause applies only to treaties later in time, or not included in that no other investment treaties or chapters are included at all. To a certain extent the Commission is aware of this problem as it has excluded the market access provisions and the investor to state procedures of the investment chapter from the scope of the MFN clause.
- To clarify the way investment protection standards have been formulated. CEEP believes that the non-discrimination clause of the investment chapter should only apply to investments already made. Therefore, the Commission should consider the exclusion of pre-admission protection in TTIP, so that investors who feel they have been treated unfairly in the process of establishing an investment cannot bring a claim on the basis of TTIP. CEEP calls for decisions on this matter to be taken in line with the future EU offer on services in order to avoid the risk of making a possible agreement on TTIP internally inconsistent.

Question 3: Fair and equitable treatment

CEEP welcomes the Commission's initiative on the general objective of clarifying the Fair and Equitable Treatment (FET) standard as a significant step towards greater protection of the foreign investors and their investments. Thus, CEEP can only agree with the presented closed list which summarizes manifest breaches. This closed list seems very reasonable and also useful to provide the investor with clear protection from unacceptable treatment by the state. Yet, article 2(f) of the reference text states, that a party breaches the obligation of FET where measures constitutes "*A breach of any further elements of the fair and equitable treatment obligation adopted by the Parties in accordance with paragraph 3 of this Article*". This introduces elements of vagueness and subjectivity into the abovementioned closed list and could therefore lead to multi-interpretations by arbitrators in an investment tribunal. Furthermore, CEEP asks for more detailed information on the frequency and on the accountability of the review process of the content of the obligation to provide FET under article 3. Indeed, if the Commission aims at making TTIP a "live" agreement that can be adapted to circumstances, the question is how parliaments, civil society and the general public will be able to scrutinize the continuous expansion of the agreement. In this case the competences and the subsidiarity principle have to be considered.

In addition, CEEP supports the Commission's approach which ensures that the standard is not understood to be a "stabilization obligation" that would prevent legal regimes of host states to change. Yet, article 4 claims that " *(…) a tribunal may take into account whether a Party made specific representation to an investor to induce a covered investment, that created a legitimate expectation upon which the investor relied in deciding to make or maintain the covered investment (…)*" this does not seem to provide the legal certainty, that national legal systems will not be circumvented by private corporations. For instance, the text refers to "a specific representation", which is a very open term. CEEP would like to know whether or not the Commission intends to include a so-called

"umbrella clause" into TTIP. Clarification on this would help stakeholders to have a better overview of host states' specific undertakings towards its foreign investors.

In other words, CEEP still sees the potential for foreign investors to attain more enforceable rights against States, in situations where a State's conduct or legislative actions have been contrary to a company's commercial interest by implementing social and environmental policies that would inadvertently decrease the company's profit. Indeed, the FET definition as proposed in the CETA investment chapter has already sparked several lawsuits, such as one by Philip Morris challenging Australian government's stricter restrictions for cigarette packaging. Defining and implementing social and environmental policies must remain under European national regulation in accordance with the treaties and should not be regulated by a transatlantic agreement.

CEEP proposes:

- That any kind of representation has to be existent in writing to be accepted as evidence by the arbitrators. In addition, FET provisions could include wording stating that an investor claiming that a state has violated a customary international law obligation has the burden of demonstrating that the obligation exists based on evidence of actual state practice and *opinio juris*, and that such an obligation may not be established solely through arbitral awards or secondary sources.
- Not to include an 'umbrella clause' into a possible agreement on ISDS in TTIP. An 'umbrella clause' would provide investors with an additional redress mechanism for the settlement of contractual disputes between them and the host state. This would consequently limit governments' right to regulate.
- To further clarify key investment protection standards and the scope of notions such as 'fair and equitable treatment' (FET) in order to provide sufficient guidance to tribunals and to limit States' exposure to a possible ISDS. Thus, FET provisions could include "an exhaustive list of State obligations under FET," as the United Nations Conference on Trade and Development (UNCTAD) has suggested.

Furthermore, a so-called 'umbrella-clause' should not be included and the definition of the 'right to regulate' for parties should be extended and included into other investment chapters.

Question 4: Expropriation

No comment.

Question 5: Ensuring the right to regulate and investment protection

CEEP notes that the Preamble of the CETA text recognizes *"the right of the Parties to take measures to achieve legitimate public policy objectives on the basis of the level of protection that they deem appropriate."* Regarding this paragraph, CEEP expresses the following suggestions:

- The well-established precautionary principle should be mentioned as such. Furthermore, referral to or incorporation of the Organization for Economic Co-operation and Development

(OECD) Guidelines on social corporate responsibility and International Labour Organization (ILO) Declaration would be of value.

- The right for states to regulate encompasses a far broader scope than *"legitimate public policy objectives on the basis of the level of protection that they deem appropriate".* Indeed, European policies are constantly evolving as they respond and react to new technological, environmental, social, economic and democratic challenges, as well as new expectations of citizens and businesses. In a democratic system, competent authorities (European, national, regional or local level) are expected to reflect these norms and wishes.
- CEEP also notes the presence of a similar paragraph in the annex on expropriation. CEEP supports the fact that similar provisions should be included for instance in articles on MFN and on FET. Indeed, expropriation is less used to attack general policies than the MFN or the Fair and Equitable Treatment (FET) standard. To be more precise, the mention of a "right to policy" principle in the preamble might be insufficient and such provisions should be a general principle of the investment chapter. CEEP considers essential that any provision proposed in the TTIP does not hinder the ability of the EU Member States to regulate in the public interest.
- CEEP calls the Commission to resist the inclusion of a so-called 'ratchet provision' into a future FTA with the US'. Such provision will significantly undermine the right for states to regulate". If there is an agreement on ISDS, this should not take away States' right to regulate. Therefore CEEP thinks that a consultative body on regulation's right within TTIP could be set up among Member States. For example, regards to the conventions of the International Labour Organisation (ILO) in Geneva, there is a advisory body composed of international lawyers that releases opinions on disputes between, States and companies and States and Non Governmental Organizations. Even if this body is 'only consultative', its opinions are often taken into account by disputing parties.
- Finally, CEEP notes that the Commission gives some room for manoeuvre and wants to give *"Parties the possibility to adopt interpretations of the investment protection provisions which will be binding on arbitral tribunals".* Yet, CEEP raises serious concerns about the arbitral body and about the transparency of the whole process (questions, 6, 8 and 12).

B. INVESTOR-TO-STATE DISPUTE SETTLEMENT (ISDS)

Question 6: Transparency in ISDS

The Commission states that "all documents will be publicly available" and "hearings will be open to the public". The Commission bases its argumentation on the new United Nations rules on transparency (UNCITRAL) and especially on Articles 2 and 3 of UNCITRAL. However, article 7 of UNCITRAL foresees several exceptions allowing arbitral tribunals to hold information confidential. According to article 7 *"The arbitral tribunal may, on its own initiative or upon the application of a disputing party, after consultation with the disputing parties where practicable, take appropriate measures to restrain or delay the publication of information where such publication would jeopardize the integrity of the arbitral process (…)".*

With regard to hearings, both the CETA and the UNCITRAL documents foresee exceptions to hold parts of hearings in private, for instance to protect the "integrity of the arbitral process" or *"confidential business information"* (Article 7(2)(a) of UNCITRAL), but also for "*logistical reasons*." A similar provision can be found in point 5 of the provided CETA document on "Transparency of Proceedings". Thus, article 6(2) of the UNCITRAL document states, that *"Where there is a need to protect confidential information or the integrity of the arbitral process pursuant to article 7, the arbitral tribunal shall make arrangements to hold in private that part of the hearing requiring such protection."* Article 6(3) says, that *"The arbitral tribunal shall make logistical arrangements to facilitate the public access to hearings (…). However, the arbitral tribunal may, after consultation with the disputing parties, decide to hold all or part of the hearings in private where this becomes necessary for logistical reasons, such as when the circumstances render any original arrangement for public access to a hearing infeasible."*

These rules apply to investor-State arbitration initiated under the UNCITRAL Arbitration Rules pursuant to an International Investment Agreement concluded on or after 1 April 2014. It is therefore difficult at this stage to assess whether or not parties have made an extensive use of the above-quoted exceptions. However, CEEP argues that an improvement of the transparency under UNCITRAL mostly depends on the composition of the arbitral tribunals (question 8) since *"Any determination as to whether information is confidential or protected shall be made by the arbitral tribunal after consultation with the disputing parties."* (Article 7(3) of UNCITRAL) and since it is in charge of allowing third-person submissions by determining *"Whether the third person has a significant interest in the arbitral proceedings"* (Article 4 (3)(a) of UNCITRAL).

Question 7: Multiple claims and relationship to domestic courts

Under question 7 the Commission states that ISDS tribunals cannot order governments to reverse measures. The provided CETA text does indeed allow the Arbitration tribunal to only impose monetary damages or restitution of property. However, CEEP is concerned that the threat of such damages or simply the threat to use ISDS tools may be enough for targeted governments to repeal measures. Previous ISDS cases demonstrate that ISDS and the arbitrational courts have ensured that countries have been subject to severe financial punishments after having for instance enacted stricter environmental laws.

Furthermore, the Commission leaves the choice for investors to choose between domestic courts and the ISDS tool. CEEP supports this approach: investors should be allowed to choose domestic courts since experience shows that the development of international arbitration mechanisms tends to favour business at the expense of the states, it is therefore likely that investors will choose the ISDS tool. Indeed, under the ISDS tool foreign investors often acquire more rights on the market, than national players, because as opposed to national legal systems, ISDS provisions are often wider and vaguer. This leaves substantial room for corporations to sue states for implementing stricter social policies, if it causes financial loss to the company, while national companies are bound by more precise national legislation that does not allow for such frivolous claims. Consequently, countries may be punished for updating social policies within their territory, should they not be agreeable to commercial interests of foreign investors. The introduction of an ISDS in transatlantic partnership could therefore be costly to Europe and force it to abandon some of its core values and principles.

On the whole CEEP does not see enough incentives in the text that "encourage the use of domestic courts" as the European Commission claims it does. On the other hand, we agree with the European Commission that the CETA text tries to address the problem of multiple parallel proceedings. The text succeeds in this respect. In order to submit a claim to arbitration, the claimant investor is barred from engaging in a parallel domestic process about the same measure. If the investor wishes to submit to arbitration, proof will have to be provided that the domestic proceeding has been completed and closed or that the investor has withdrawn from the proceeding. Moreover, the investor must waive the right to initiate such proceedings. In our view, this is a positive development. However, we do not consider that this favours or encourages domestic courts in any way.

Question 8: Arbitrator ethics, conduct and qualifications

The EU claims that it *"will introduce specific requirements in the TTIP on the ethical conduct of arbitrators, including a code of conduct"*. However that code of conduct is not available yet. According to the CETA text, this code of conduct shall be adopted by a join committee *"no later than two years after the entry of the Agreement."* CEEP finds it consequently difficult to assess the credibility of EU's intentions.

CEEP also notes that this code of conduct *"may address topics including:*

- *disclosure obligations;*
- *the independence and impartiality of arbitrators; and*
- *confidentiality."*

CEEP thinks that issues such as "the independence and impartiality of arbitrators" should be addressed by the code of conduct because they have been identified as problematic. However, we cannot know whether this Code will adequately deal with these problems because the adoption of the Code is postponed by up to two years after the entry into force of the agreement. In our view, the Code of Conduct should be finalized along with the rest of the investment text. Given the uncertainty as to whether this Code will ever be finalized and the uncertainty regarding its content, we cannot, at this point in time, agree with the European Commission that steps have been taken to address the issue of arbitrator impartiality and independence. Any assessment of impact of the Code would be mere speculation.

What is more, the Commission states that *"This code of conduct will be binding on arbitrators in ISDS tribunals set up under TTIP".* CEEP finds no clear evidence in the text that this code of conduct will be binding. On the contrary, the Commission makes a clear reference to the International Bar Association Guidelines on Conflicts of Interest in International Arbitration (Article x-25(6)). CEEP reminds the Commission that those guidelines are a general code not elaborated for ISDS.

Regarding the creation of a roster, it is true that to date investment treaties often do not provide for a "roster" of arbitrators, but the ICSID system does use a roster system under which the Secretariat maintains a list of Conciliators and of Arbitrators, so the idea is actually not new. Also, the roster approach at ICSID has not helped mitigate concerns of impartiality and independence of arbitrators.
CEEP is of the view that the kind of roster approach proposed in the CETA will also fail to address these concerns. As for ICSID, the first two arbitrators under CETA are unilaterally nominated by the investor and the state and there is no need whatsoever to choose an arbitrator from the roster. The roster only comes into play where the parties fail to appoint the presiding arbitrator within three months of the submission of the claim, or fail to appoint their own arbitrator (this latter situation is not expected to be common under CETA). This is very similar to the ICSID roster system, where the presiding arbitrator is only chosen from the roster when one of the arbitrators is not nominated. The roster is therefore only a backup and does not have the power of an exclusive roster for all the arbitrators fulfilling strict conditions of experience, independence and impartiality. As a consequence, all the problems resulting from party appointments, such as arbitrators focusing more on pleasing the nominating parties and being re-appointed in future cases, are not resolved through the roster system proposed in the CETA draft.

To summarize, CEEP asks for:

- The finalization of the code of conduct along with the rest of the text on investment protection. This code of conduct should be binding and should deal with issues such as "the independence and impartiality of arbitrators" in order to improve the transparency and legitimacy of the arbitral tribunals.
- A more extensive use of the roster list. The roster list should not be a last resort remedy. On the contrary, the roster should become exclusive and the listed persons should fulfill strict conditions of experience, independence and impartiality. In case a roster system is implemented, parties should be involved in the choice of the conciliators and arbitrators in order to guarantee a fair and transparent process.

Question 9: Reducing the risk of frivolous and unfounded cases

No comment.

Question 10: Allowing claims to proceed (filter)

No comment.

Question 11: Guidance by the Parties (the EU and the US) on the interpretation of the agreement

No comment.

Question 12: Appellate Mechanism and consistency of rulings

The idea of introducing an appellate system is a good one in our view. As we can see from the WTO experience, the WTO appellate mechanism is working well. The Appellate Body is well respected, and has contributed to a more predictable trading system through its clarifications regarding key questions of interpretation. The result has not only been better law and consistency but also improved compliance and trust in the system. Thus, the European Commission states that it aims at establishing an appellate mechanism in TTIP. Yet, the CETA text is only an incentive to the Committee on Services and Investment *"to provide a forum for the Parties to consult on issues to (…) "whether, and if so, under what conditions, an appellate mechanism could be created under the Agreement".* It might therefore be taken as an indication that such a provision might fail to materialize. Certainly, at this stage, we cannot conclude that the ISDS in CETA has solved the problems relating to lack of consistency, predictability, and legal correctness just by including the possibility of establishing an appellate mechanism.

In case of the creation of an ISDS tool in TTIP, CEEP asks for:

- The creation of a real appellate mechanism largely based on the WTO appellate mechanism model.
- A deadline for the delivery of the appellate report itself. Indeed, the draft CETA text only provides the deadline of filing an appeal and the time-period of the adoption of the appellate body's report by the tribunal, omitting the timetable for the delivery of the appellate report itself. This is a vacuum to be filled since it could delay the whole appellate process.
- Relevant provisions regarding the composition of the appellate body. The WTO Arbitral Body model, based for instance on collegiality, could be employed in case of ISDS in TTIP.

C. General assessment

In addition to its previous comments, CEEP would like to make the following remarks and statements:

- CEEP is concerned about the final impact of the EC Consultation on modalities for investment protection and ISDS on negotiation on TTIP.
- The Commission has clearly identified and defined a number of issues raised by CEEP as well as by numerous stakeholders. However, CEEP notes several discrepancies between the Commission's approach and the CETA text. Furthermore, CEEP notes that negotiations on ISDS in CETA are still ongoing and that the text might be consequently amended. CEEP hopes that the final result of the negotiation on TTIP will reflect stakeholders' concerns and invites the Commission to stand firm in the negotiations.
- The European Commission statement does not address the role of the CETA as a forerunner to the TTIP negotiations. It will, of course, be much more difficult for the EU to conclude an agreement with the United States that does not include an ISDS clause if the CETA does

contain one. However, regarding the CETA, the European Parliament stated in its resolution from 8 June 2011 that the negative list approach in the CETA should be seen as a mere exception. Thereby, the CETA should not serve as a precedent for future negotiations.

- CEEP agrees with the text voted by the European Parliament on Financial responsibility linked to investor-state dispute settlement tribunals established by international agreements to which the EU is party, when it states, that *"Union agreements should afford foreign investors the same high level of protection as Union law and the general principles common to the laws of the Member States grant to investors from within the Union, but not a higher level of protection. Union agreements should ensure that the Union's legislative powers and right to regulate are respected and safeguarded"* (point 4 of the preamble). CEEP calls for the full implementation of these principles, especially when it comes to health and environmental policies.
- CEEP notes with satisfaction that, in Questions 2 and 5 of the consultation, the European Commission explicitly foresees a "carve-out" of the audiovisual sector from investment protection. CEEP invites the Commission to carefully cater, in application of its mandate, for an effective exclusion of audiovisual services - irrespective of the platform used, the technology, or the bundling with other services- from a future agreement.
- CEEP could in principle support the inclusion of investment protection chapters in recent and forthcoming EU FTAs, provided that this protection is not traded against market-opening and does not endanger services of general interest as well as European standards. CEEP thus accepts the need for an enforcement mechanism and for investment protection. Such an enforcement mechanism should provide for a fact based and neutral dispute resolution mechanism, in accordance with established and recognized law enforcement principles, e.g. possibilities of remedies, public disclosure of information and holding of public hearings, creation of a real appellate mechanism and of a binding and exclusive code of conduct for arbitrators. Concerning the provisions on the protection of investors, CEEP is concerned that there may be significant potential for harm in allowing foreign investors to bypass domestic courts and specific contract-based remedies in favour of treaty arbitrations that include elements going well beyond the rights domestic investors have. Therefore, CEEP asks the Commission to pay special attention to the scope of the definition of 'investment', to clarify the way investment protection standards have been formulated by ensuring, for instance, that the non-discrimination clause of the investment chapter only applies to investments already made. Furthermore, a so-called 'umbrella-clause' should not be included and the definition of the 'right to regulate' for parties should be extended and included into other investment chapters, such as the 'Most favoured Nation' clause and the 'Fair and Equitable Treatment' clause. Clear references to the ILO conventions and to the Organization for Economic Co-operation and Development (OECD) Guidelines on social corporate responsibility would help safeguard European social standards. In addition, the local and regional self-government (Article 4(2) TEU), the principle of subsidiary and the principle of proportionality (Article 5 (3)) shall not be undermined by special rights for private international investors. The decision-making and regulatory right of the regional and local authorities in the area of public services must be guaranteed. Moreover, incentives for investors to choose a national court could be further developed. Finally, the Commission should first assess whether all those kinds of guarantees could not be best achieved within current legal system frameworks.