Report on Panel 1: Should investment disputes be submitted to international arbitration or to a permanent investment court?

Moderator: Nabil Elaraby, Chairman, Board of Trustees, Cairo Regional Centre for International Commercial Arbitration

Speakers: Marc Bungenberg, Chair of Public Law, Public International Law and European Law, Saarland University, Saarbrücken

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Nikos Lavranos, Secretary-General, European Federation for Investment Law and Arbitration, Brussels

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In his introduction, **Nabil Elaraby** noted that the international arbitration community had been discussing investor-state dispute settlement (ISDS) reform for many years. The existing system, he observed, had given rise to doubts over the consistency of decision making and the impartiality and independence of party-appointed arbitrators. Further, the problem of inconsistent decisions by ad hoc annulment committees was compounded by the lack of any unified mechanism allowing decisions to be appealed and their consistency and correctness checked. The present ISDS system also allowed arbitrators to wear dual hats as counsel and arbitrators (so-called "double hatting"), which had given rise to conflicts of interest.

Dr. Elaraby explained that there were two broad sets of proposals for reforming ISDS. The first was to keep the current ISDS regime, but to add an appellate mechanism to avoid inconsistency and uncertainty, and to change the method of appointing arbitrators so that parties are no longer

involved in the appointment process. The second, and more radical, suggestion was to replace the current system of ISDS altogether with a permanent investment court, where publicly-appointed, independent, professional judges would decide cases in a transparent manner and in public hearings. The European Union (EU) was the strongest proponent of such a system, which was envisaged in the Comprehensive Economic and Trade Agreement (CETA) between Canada and the EU and in the EU's free trade agreements with Singapore and Vietnam. Dr. Elaraby questioned, however, whether a permanent investment court would cure the various shortcomings of the existing ISDS regime.

Marc Bungenberg spoke on how a permanent investment court system might work in practice, how it would be created, what it would look like, and the challenges posed by the creation of such a court.

He began by referring to the recent discussions of Working Group III of the United Nations Commission on International Trade Law (UNCITRAL) in Vienna, where ISDS reform was discussed. He said that the "elephant in the room" was whether states would move in the direction of a permanent investment court. The current ISDS system was strongly criticized, particularly in Germany and Austria, and by NGOs and other organizations in the EU, for "double hatting", the lengthiness and costliness of proceedings (the total cost of investment arbitration proceedings, including parties' legal costs, averaging in excess of USD 8 million), and the inconsistency of decisions by ad hoc tribunals. The EU's answer to these criticisms was to move away from ad hoc arbitration towards a permanent, two-tiered structure consisting of a tribunal of first instance and an appeals tribunal.

According to Professor Bungenberg, the proposal to create a permanent investment court did not necessarily mean that the current ISDS system did not work. Rather, he argued, the addition of a permanent investment court system that included an appeals mechanism could result in

greater substantive coherence, predictability, and legal certainty, which would contribute to the acceptance of investment decisions.

He suggested that a permanent investment court could be created by a convention similar to the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration (the "Mauritius Convention"), leaving intact the existing network of predominantly bilateral investment treaties (BITs) with their standards of protection. As an international, treaty-based organization with its own organs and legal personality, the court would be completely independent of ICSID and the Permanent Court of Arbitration, although there was nothing to stop it sharing the infrastructure of those institutions.

Professor Bungenberg then presented an overview of the composition of a permanent investment court. A plenary body would be responsible for appointing judges and setting the court's budget. The judges would be independent, highly qualified – particularly in international, economic, and public/constitutional law – and would work full-time. He saw two advantages in having permanent judges: first, they would help to ensure that substantive standards of international investment law are applied consistently; and second, the risk of conflicts of interest would be avoided as "double hatting" would not be possible. The independence of the judges would be protected by restricting their appointments to a single term (of eight to ten years).

With respect to diversity, Professor Bungenberg pointed to the International Tribunal for the Law of the Sea and the International Court of Justice – consisting of judges broadly representative of the legal systems and regions of the world – as reason to believe that a similarly diverse composition could be achieved within a permanent investment court.

Professor Bungenberg said that a permanent investment court could have other benefits. For example, the transparency requirements of the UNCITRAL Rules on Transparency in Treaty-

based Investor-State Arbitration could be incorporated into the procedural rules of a permanent investment court. This would ensure the publication of procedural documents, open hearings, and the opportunity for *amici curiae* to make submissions, all of which would strengthen the court's legitimacy.

On the question of costs, an Investment Advisory Centre (IAC) could be established as an independent body to lighten the financial burden for small and medium-sized businesses and developing countries by helping to prevent and settle disputes and by offering legal advice during any arbitration. With regard to the length of the proceedings, they would be time-limited in both the tribunal of first instance and the appeals court, and only in exceptional cases would an extension be permitted; while the hearing of cases by full-time judges should itself help to make proceedings shorter than in ad hoc cases.

One of the problems of a permanent investment court was the recognition and enforcement of the awards rendered by such a body, which, as currently envisaged, was not compatible with the enforcement provisions of either the ICSID or New York Conventions. Professor Bungenberg argued that the enforcement mechanism of the ICSID Convention would not apply to the awards of a permanent investment court and that the decisions of a permanent investment court might not qualify as arbitral awards as defined in the New York Convention. Although the statute of the permanent investment court could provide that its decisions should be deemed arbitral awards within the meaning of the New York Convention (in similar fashion to Article 8.41(5) of CETA), it was currently unclear whether such a provision would be accepted as binding by the domestic courts of enforcement states, particularly those that had not adhered to the multilateral treaty providing for a permanent investment court. For these reasons, it would be preferable for a permanent investment court to have its own enforcement mechanism. Professor Bungenberg's conclusion, therefore, was that, although a permanent investment

court might potentially offer several advantages over the present system, the establishment of such a court also raised a number of problems.

Like the previous speaker, **Markus Burgstaller** discussed the concerns raised within UNCITRAL Working Group III and the various legal and practical issues associated with an investment court system.

He noted that Working Group III had identified three main areas of concern within the existing ISDS framework, namely, consistency and coherence among arbitral decisions, the independence and impartiality of arbitrators, and the excessive length and cost of proceedings. He said that there were other legitimate concerns, including a perceived pro-investor bias, a lack of transparency, the "regulatory chill" of arbitral decisions on a state's right to regulate, and forum shopping by claimant investors.

Some states, like South Africa, had responded by withdrawing from the system, with the result that foreign investors were forced to litigate their disputes in domestic courts. The EU, on the other hand, had taken a different line by proposing the establishment of an investment court system, but this proposal had received from certain other states, including Japan and the United States, a response that Dr. Burgstaller described as far from enthusiastic.

Echoing Professor Bungenberg's earlier comments, Dr. Burgstaller noted how the EU's proposals sought to address the main concerns of Working Group III. An investment court could create a body of binding precedents and more consistent interpretations of substantive protections, while appeals on issues of fact and law could provide a means of improving predictability and remedying incorrect decisions. Further, the fact that judges would serve on a permanent rather than an ad hoc basis would help to guarantee their independence and impartiality, as would a code of conduct and the rotation of judges to ensure that all candidates

had an opportunity to sit on cases. A permanent investment court could also be an antidote to the excessive length and cost of proceedings as it should weed out frivolous claims at the outset.

However, Dr. Burgstaller said that the EU's proposals could be criticized on a number of important grounds.

First, the idea that an investment court would increase consistency was premised on the assumption that the court would be ruling on the basis of a common investment treaty. The opposite was true, however, and no matter how great the court's efforts to be consistent in its decision making, it would inevitably be frustrated by the large number of different international investment treaties it would have to apply and the diverse substantive standards laid down in those treaties. Any attempt to achieve widespread consistency would thus first require a convergence of procedural and substantive rules, which was unlikely in the short term as the international community had divergent views on the subject.

Second, the fact that judges' retainers would be paid by the states alone would make the judges economically dependent on the states, which could prevent them from being perceived as independent and impartial. Furthermore, "double hatting" could continue, since members of the investment court might also act as members of tribunals under other treaties lying outside the jurisdiction of the investment court.

Third, Dr. Burgstaller pointed out that the introduction of appellate proceedings would do nothing to cure the excessive duration and cost of proceedings. On the contrary, empowering appeals tribunals to correct errors of fact and law would necessarily lead to lengthier proceedings.

Fourth, as Professor Bungenberg had said, a permanent investment court system would cause difficulties with respect to enforcement under the ICSID and New York Conventions. One of the strengths of the existing ISDS system was the effectiveness of enforcement under both the

ICSID Convention, with its self-contained enforcement mechanism, and the New York Convention. Under an investment court system, on the other hand, enforcement remained an unresolved issue, as it was difficult to see how an award rendered by a permanent investment court could be enforceable under either the ICSID Convention or the New York Convention.

For Dr. Burgstaller, the "elephant in the room" was the legal uncertainty surrounding CETA. He noted, however, that the Court of Justice of the European Union (CJEU) had been requested to give an opinion on CETA's compatibility with EU law. That opinion was eagerly awaited, but it was currently unclear which way the CJEU would rule.

Dr. Burgstaller drew the conclusion that an investment court system was not a panacea. Indeed, if set up in isolation and in haste, it could create more problems than benefits.

Dr. Burgstaller went on to discuss alternative, and more practical, approaches to reform. He argued that reform that did not involve the creation of a new permanent investment court system would be more productive and beneficial for all stakeholders. A far more important step would be to increase the transparency of the system by publishing more awards of investment tribunals, which would allow arbitrators to follow the reasoning of awards in cases similar to their own. The Mauritius Convention – and its focus on transparency – was already a step in the right direction, he said. He also encouraged greater use of pre-arbitral mechanisms, including mediation, to reduce costs and delay.

Dr. Burgstaller said that discussions on reform were still ongoing. At its next session in New York in April 2019, UNCITRAL Working Group III would be discussing what, if any, reforms ought to be made to ISDS, while ICSID was also in the process of amending its arbitration rules.

He concluded by saying that if arbitral institutions were to act more robustly in enforcing procedural rules, including on time limits, and in ensuring the independence of arbitrators, that would strengthen the system as a whole.

Nikos Lavranos considered the concept of a permanent investment court to be a backlash – particularly in Europe – against globalization, multinational corporations, and the proposed Transatlantic Trade and Investment Partnership (TTIP). The move towards such a court marked a shift towards protectionism, nationalism, and regulatory intervention by host states, following the 2008 financial crisis.

Dr. Lavranos argued that proposals for a permanent investment court were a political, not a legal, issue. The problem had emerged as a result of host states' increasing dislike of the decisions rendered by arbitral tribunals and their objection to being straitjacketed by some 3,000 BITs. That said, statistics showed that states continued to win more cases than investors, and were also increasingly successful in escaping payment orders in awards against them by invoking state immunity or initiating set-aside proceedings.

Dr. Lavranos observed that, in addressing the ISDS problem, states had become fixated on making it as hard as possible for investors to enforce their rights, both procedurally and substantively, and on the idea of a permanent investment court, instead of trying to reduce the scope of ISDS claims by tackling corruption and focusing on rule of law standards. A clear example of this trend was the renegotiated North American Free Trade Agreement (NAFTA) between Canada and the United States, in which ISDS was virtually eliminated.

Dr. Lavranos noted that, under the EU-led investment court proposal, states would be able unilaterally to select judges of their choosing, and have some sway over their conduct as they would be unlikely to reappoint judges whose past rulings they disagreed with. Dr. Lavranos argued that the recent World Trade Organization (WTO) Appellate Body crisis, with respect

to the reappointment of certain members to the WTO's Appellate Body, demonstrated that states were all too willing and able to "hijack" judicial bodies. He considered that the omission thus far of any provisions to ensure transparency in the selection of judges made it questionable whether the judges of a permanent investment court could be more independent and impartial than arbitrators currently are.

Dr. Lavranos referred in passing to the restrictive definitions of investor and investments in treaties involving the EU. The closed fair and equitable treatment (FET) list reduced FET to the standard asserted in the 1926 *Neer* case, in which the Claims Commission established pursuant to the 1923 USA-United Mexican State Convention held that:

> [T]he treatment of an alien, in order to constitute an international delinquency, should amount to an outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency. Whether the insufficiency proceeds from deficient execution of an intelligent law or from the fact that the laws of the country do not empower the authorities to measure up to international standards is immaterial.

Dr. Lavranos argued that in the draft TTIP, EU-Singapore and EU-Vietnam trade agreements, the long list of exempted sectors and the acceptance of indirect expropriation without compensation, except in rare circumstances, would limit claims by foreign investors against host states to acts of a most outrageous kind, which would be very difficult to prove.

Dr. Lavranos was also critical of the introduction of an appeals process. In practice, this would give states, in particular, a second bite of the apple, while increasing costs and delaying proceedings. Most investors, he argued, would not have the money or the resources required for long, drawn-out appellate proceedings. He also warned that increased transparency, with

the possibility of *amici curiae* interventions, was likely to politicize disputes and demonize claimant investors. Reiterating the comments of Professor Bungenberg and Dr. Burgstaller, Dr. Lavranos pointed out that awards rendered by an investment court would not qualify as awards under the ICSID or New York Conventions, which would reduce the court's effectiveness.

Dr. Lavranos doubted that a permanent investment court system could ever constitute an efficient, fair and independent dispute settlement forum. He saw it rather as an "expensive charade and window-dressing exercise," a gesture towards ISDS by host states, whose real purpose was to escape their international obligations and get away with behavior in clear breach of BITs and ultimately to give their domestic courts sole jurisdiction over foreign investors, as amply demonstrated by the renegotiated NAFTA. The real problem, in Dr. Lavranos's view, was the unfair treatment of foreign investors resulting from deficiencies in domestic systems, corruption, and political interference. States would do better to focus on improving domestic rule of law standards rather than waste money and manpower on a permanent investment court.

Dr. Lavranos concluded by asking why it was that the top five countries of the World Justice Project 2017–2018 Rule of Law Index were Denmark, Norway, Finland, the Netherlands, and Sweden, and that those countries had never had an ISDS case brought against them in fifty years. The answer, he suggested, was simple: if states want to avoid ISDS claims, they need to improve their rule of law standards and not make life unnecessarily difficult for foreign investors.

Nassib G. Ziadé took the view that the safest and most effective way to address the flaws in the current ISDS system was to reform rather than replace the system. He endorsed the comments of his fellow panel members on the various shortcomings of the existing ISDS regime. In his view, the most pressing concern was the issue of conflicts of interest. He noted that many arbitration practitioners repeatedly wear several hats simultaneously as arbitrator,

counsel and expert in cases involving overlapping issues. Further, they routinely appoint each other and regulate their own activities. He considered that the situation was not helped by the reluctance of arbitration institutions to issue basic guidelines on conduct and their failure to handle appointment and challenge procedures with the level of transparency one would expect.

While an investment court might appear to allay some concerns, Professor Ziadé argued that it did not adequately address the main flaws and could even create new problems. While he sympathized with the unease felt by many states, he suggested that the search for solutions was misdirected.

According to Professor Ziadé, it would be hard to avoid the impression of a permanent investment court being biased in favor of states. Unlike the existing ISDS system, where the disputing parties participate on an equal basis in the composition of an arbitral tribunal, an investment court would vest in the states the exclusive power to appoint judges. Even if states were to give investors the opportunity to choose judges from a roster, that process would still be slanted in favor of the respondent state as that state would have participated in the creation of the roster. Judges might feel indebted to the states that appointed them and were ultimately responsible for their remuneration, and some may even fear not being reappointed if they did not rule in the states' interests. Professor Ziadé pointed to the complications caused by the reappointment of certain members of the WTO's Appellate Body as proof of the extent to which judicial appointments to a permanent investment court could become politicized.

Professor Ziadé argued that giving states the unilateral power to appoint judges could have unintended consequences. For example, foreign investors might be discouraged from investing in countries that join the court, or they might make their investments conditional upon the insertion of an arbitration clause in the investment contract, or upon a higher rate of return to compensate for increased risk.

Besides these concerns, an even more fundamental problem, in Professor Ziadé's view, was that the proponents of a permanent investment court were essentially seeking to transpose the WTO dispute settlement mechanism onto international investment law. Professor Ziadé predicted that this was likely to prove unworkable because the two fields had very different bodies of law and stakeholders. He quoted the following words from the 2016 Lalive lecture delivered by Sir Michael Wood, whose background was hardly suggestive of pro-investor bias:

> I would also point out that, notwithstanding that the European Commission papers and proposals are quite detailed, it is far from clear how they would work in practice. They seem to be inspired to some degree by the WTO system. But inter-State trade disputes concerning the interpretation and application of multilateral WTO treaties are hardly comparable to investor-State investment disputes under more than 3,000 bilateral investment treaties, each with its different wording and negotiating history.

If an investment court was not a viable solution, then what was?

One solution might be to establish an appellate mechanism within each of the institutions that administer investment arbitration cases, or, alternatively, to create a single, centralized appellate mechanism within one of those institutions. However, Professor Ziadé cautioned that ISDS was already criticized for being slow and costly, and adding an additional layer of proceedings would only exacerbate the problem. He expressed the fear that appeals could become the norm, with both losing investors and states bringing appeals as a matter of course. This could have a particularly harmful impact on developing states subject to severe budgetary constraints and on small and medium-sized investors, thereby adding to the existing imbalances among investors and states.

Professor Ziadé questioned whether an appeals mechanism was capable of embracing some 3,000 highly diverse bilateral and multilateral treaties, and he doubted that it would address the

problem of inconsistent investment awards and decisions as an appellate body could reverse a decision if it construed a treaty or contract differently, rather than simply on the basis of factual or legal incorrectness.

As an alternative to an appeals mechanism, Professor Ziadé argued that the interpretation of contested treaty provisions could be better harmonized through the creation of joint committees that would coexist alongside arbitration tribunals, and he noted that such joint interpretive bodies already existed under NAFTA and CETA.

Professor Ziadé then considered how the annulment committee system established pursuant to Article 52 of the ICSID Convention might be reformed. He said that he continued to argue for a pool of arbitrators dedicated exclusively to handling annulment proceedings, as this would help to ensure consistency in the application of the ICSID Convention and Rules by annulment committees.

In response to the complaint by some states that annulment committees under the ICSID system could annul awards only on very limited grounds, Professor Ziadé said that states could insert in investment treaties referring to ICSID arbitration additional grounds that would apply in proceedings initiated pursuant to such treaties. This was an option that deserved serious consideration at the very least, he insisted.

On the issue of conflicts of interests, Professor Ziadé urged arbitration institutions not to shy away from issuing internal codes of conduct applicable to their staff and procedures, and external codes applicable to the arbitrators and counsel who act in the cases they administer. If arbitration institutions are to take on additional responsibilities in the selection of arbitrators to counter the perceived lack of independence and impartiality of party-appointed arbitrators, then it was important, Professor Ziadé maintained, that they undertake the reforms necessary to ensure the transparency of their procedures.

To summarize, Professor Ziadé said that the establishment of a permanent investment court, which would be a true leap in the dark, was not the way to remedy the imperfections of investment arbitration. The choice, he said, was not between unconstrained, self-regulating investment arbitration exposed to the vagaries of arbitration practitioners, and a permanent investment court with ill-defined boundaries and a hastily adopted statute. Rather, the way forward was carefully to circumscribe investment arbitration and prevent specialized arbitration institutions from delegating their regulatory role to arbitration practitioners. Professor Ziadé pleaded for investment arbitration thus reformed to be given a chance to prove itself.

Professor Ziadé expressed the consternation he felt upon hearing some organizations and individuals claiming to represent the views of developing countries when advocating the creation of a permanent investment court. He insisted that developing countries had diverse views and that no one had a monopoly on representing those views. While the idea of creating a permanent investment court might initially appear attractive to developing countries, it was Professor Ziadé's view that, in the long term, the creation of such a court would prove not to be in the best interests of developing countries.

In conclusion, Professor Ziadé compared the predicament of the existing investment arbitration system to that of a seriously ill patient. While we may wish to consider changing the provider of care or the treatment protocol, our goal, he said, should be aggressively to address the symptoms without killing the patient or sacrificing quality of life. It was Professor Ziadé's view that there were still many remedies that had not yet been administered and that had every chance of being successful, avoiding the need to administer a potentially lethal dose of medication.