

Far from being a threat to European democracy, the EU-US free trade deal is an ideal opportunity to reform controversial investment rules and procedures

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*The EU and the United States are currently in the process of negotiating a free trade area, the Transatlantic Trade and Investment Partnership (TTIP). **Robert Basedow** writes on criticism over the potential inclusion of ‘investor-state dispute settlement’ procedures in TTIP, which some commentators and academics have argued could undermine democracy on both sides of the Atlantic. He argues that rather than being seen as a threat to democracy, the TTIP negotiations should instead be seen as an opportunity for reform, and that maintaining the status quo could prove to be a greater threat to democracy and the rule of law in the long-term.*



During recent months, policy-makers, media and civil society have engaged in a heated debate over the merits of the planned Transatlantic Trade and Investment Partnership (TTIP) between the EU and the United States. The planned investment chapter is particularly controversial. The chapter is likely to contain investment liberalisation, post-establishment treatment and protection provisions, and to provide for [investor-state dispute settlement](#) (ISDS).

Critics lament that the planned ISDS provisions will enable foreign investors to sue the Member States before supranational arbitration tribunals for the annulment of social, health or environmental protection laws, inflicting high costs on investors as well as high compensation payments. Critics stress that in comparison to national courts, these arbitration tribunals lack accountability, legitimacy and transparency. Investment arbitration as envisaged under TTIP arguably challenges the rule of law, limits states’ right to regulate and to pursue public policies and thus ultimately undermines European and American democracy. The Guardian therefore characterised the envisaged investment chapter of TTIP as a ‘[full-frontal assault on democracy](#)’.

Are these concerns justified? Will TTIP harm European and American democracy and the rule of law? TTIP is actually unlikely to considerably change the status quo. The Member States of the EU and the United States have signed some 1,300 bilateral investment treaties with third countries, which are very similar in content to the planned investment chapter of TTIP and provide for investor-state dispute settlement. The US and the Member States are thus already fully exposed to all risks emanating from investment arbitration. And even though most Member States have not signed such bilateral treaties with the United States, US investors can already easily launch arbitration proceedings against the Member States today.

Why is that? Many Member States have concluded bilateral treaties with financial hubs like Hong Kong or Singapore. US investors, which do have holdings in these jurisdictions, have the right to launch arbitration proceedings under the relevant bilateral treaty between these hubs and the Member States.



Protest against TTIP, Credit: Mehr Demokratie (CC-BY-SA-3.0)

[Philip Morris Asia Ltd](#)

[vs Australia](#) is a case in point. Australia and the US never concluded an agreement providing for investor-state dispute settlement. The American tobacco giant nevertheless managed to launch an arbitration proceeding attacking Australia's new tobacco plain packaging legislation through its Hong Kong-based Asia holding under the Hong Kong – Australia bilateral treaty. It is thus fair to say that the investment chapter of TTIP is unlikely to create new risks for Europe and the United States and that the non-inclusion of an investment chapter into TTIP will preserve an already critical status quo.

The heated debate on the investment chapter and notably ISDS provisions, however, finally puts the spotlight on the many lacunas of international investment agreements and investment arbitration. Even investment lawyers do not deny that many aspects of these agreements and investment arbitration are critical and need reform. TTIP offers an opportunity to finally tackle these shortcomings. The [predicted humble economic benefits](#) of TTIP – a maximum 0.5 per cent of GDP – underscore that the agreement is primarily about setting the regulatory agenda of world trade for future decades. The underlying idea is that the American and European economies jointly represent such a large share of global GDP that third countries will emulate regulatory approaches taken under TTIP. As such, TTIP is the right forum to launch a reform of the international investment regime.

Which aspects and provisions of international investment agreements and ISDS are so controversial and arguably detrimental to the rule of law and democracy? It is helpful to distinguish between the substantive and procedural provisions under typical international investment agreements. The substantive provisions enumerate the rights of investors and states under these agreements, whereas the procedural provisions regulate how substantive provisions can be enforced. The substantive provisions are hardly controversial. They reflect core principles of the rule of law. The agreements stipulate, for instance, that states can only expropriate for public policy purposes, on the basis of non-discrimination, due process and against payment of an adequate compensation for losses.

The only grievance occasionally voiced regarding the standard substantive provisions of such agreements is that they are often spelled out in too little detail, which leaves arbitration tribunals significant room for interpretation. The term 'indirect expropriation' illustrates this concern. Many international investment agreements remain vague regarding this term. They merely indicate that acts or regulations having an effect equivalent to outright expropriation should qualify as indirect expropriation and thus require states to pay compensation for losses. Some arbitration tribunals thus endorsed rather broad definitions leading to unexpected awards and costs for states. Policy-makers should thus ponder over spelling out the substantive provisions of TTIP in greater detail in order to avoid surprises and an unintended limitation of states' right to regulate.

Most criticisms regarding international investment agreements concern procedural provisions related to investor-state dispute settlement. Critics lament, for instance, that arbitration proceedings take place in great secrecy. Often the general public does not even know about the existence of claims or lacks any detailed information about their content. Taking into consideration that many arbitration proceedings indeed challenge laws and regulations, the lack of information is highly problematic in democracies.

TTIP might indeed strike new paths in this domain by rebalancing the interests of investors and/or governments in keeping arbitration proceedings secret and the rights of citizens to inform themselves. TTIP might for instance oblige arbitration proceedings to make use of a new set of [transparency rules](#) for investment arbitration elaborated in [UNCITRAL](#), which strengthens the right to information. Critics, moreover, often complain about the lack of legitimacy and accountability of arbitration tribunals. Such tribunals are typically composed of three senior lawyers, who may work at the same time as arbitrators in one case and as legal councillors in another case. This creates potential conflicts of interests.

Policy-makers can address this shortcoming of arbitration tribunals under TTIP by prohibiting arbitrators to assume these two roles within a certain timeframe. What is more, TTIP may introduce a roster of senior national judges, which may act as arbitrators in TTIP-related cases. Such innovations would enhance the legitimacy and accountability of investment arbitration. TTIP might, moreover, impose certain conditions on investors seeking arbitration in order to limit the number of cases and frivolous claims, and to prevent legal forum shopping.

Investors occasionally pursue a claim through different legal fora like national courts or arbitration until their interests are served. Such behaviour is costly for states and undermines the rule of law. TTIP might oblige investors to have recourse to only one dispute settlement forum or require investors to exhaust local remedies before turning to arbitration. Such a clause might be particularly helpful in fighting so-called frivolous claims, which investors only file in order to discredit host countries in the eyes of global business.

Finally, critics also deplore that no appellate body exists, which could review controversial awards and ensure jurisdictional coherence. It is indeed noteworthy that international investment law is characterised by the absence of a codified body of law, a supervising court or a binding doctrine of precedence, which do ensure jurisdictional coherence in other areas of international law, civil or common-law systems. The establishment of a global appellate body would require multilateral action. TTIP could nevertheless document the US and EU's support for such a step by providing for recourse to a future appellate body.

Overall, TTIP constitutes a rare opportunity to trigger a reform of international investment agreements and investment arbitration. An indiscriminate rejection of transatlantic investment disciplines, however, would preserve the status quo, which might prove to be a greater liability for European and American democracy and rule of law than a progressive investment chapter under TTIP.

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