The Right to Regulate: Towards a New Regulatory Paradigm under Recent Free Trade Agreement Investment Chapters?

A Dissection of the Trans-Pacific Partnership, Canada-EU CETA and Singapore-EU FTA

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New Lengthier Treaties

- Trans-Pacific Partnership (TPP)
  - 12 nations: Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, US, Vietnam
  - Scrubbed, but not yet final, text: Nov 2015
  - **30 chapters / 6000 pages**
    - compare to *e.g.* 2014 Myanmar-Israel BIT: only 17 Articles; 13 pages
- Canada-EU Comprehensive Economic Trade Agreement (CETA)
  - Final scrubbed text: Feb 2016; 1600 pages
- Singapore-EU (SEUFTA)
  - Latest version: May 2015; 17 Chapters, multiple annexes

What are States doing to enhance their Right to Regulate?

- Lengthier, more complex, precisely drafted treaties
- Enshrining ‘right to regulate’ in preamble, definitions, substantive provisions (standard of treatment, indirect expropriation, national treatment)
- Codifying customary international law rules
- Giving further direction to tribunals → a richer context for interpretation & reducing arbitral discretion
- Rejecting certain approaches taken by prior tribunals
- Harmonizing procedural & substantive rules, irrespective of choice of applicable arbitral rules (open hearings & transparency)

Why? Problems 'Right to Regulate' Aims to Correct

- Conflicting decisions on similar / identical points of law
- Conflicting approaches to, and weaknesses in, arbitral interpretative methodology → varying quality in coherence of legal reasoning
- skeletally-drafted / generally worded treaties give arbitrators broad discretion → potential broad or idiosyncratic treaty interpretations
- "flat" system (no centralised form of review -- until CETA & EU-Vietnam International Investment Court is enacted)
- alleged lack of sensitivity to the vital public and sovereign interests involved

The Media has picked up on the Problem

Is democracy threatened if companies can sue countries?

By Michael Robinson
BBC News

31 March 2015 | Business

Protesters in London demonstrating against the Transatlantic Trade and Investment Partnership (TTIP), a proposed new EU-US trade treaty

Those protesting against the Transatlantic Trade and Investment Partnership (TTIP), the proposed new trade treaty between the European Union and the United States, are part of a growing international opposition to pacts that allow multinational companies to sue governments whose policies damage their interests.

Opponents claim this right, known as investor-state dispute settlement (ISDS), poses a threat to democracy.

So have some Arbitrators…

Sebastian Perry, 'Stockholm: Arbitrator and counsel: the double-hat syndrome' (15 March 2012), 7 Global Arbitration Review 2, accessed online at corporateeurope.org

Realities of the Current Regime

- Rapid growth: + 3,200 BITs
- Claims often challenge States' regulatory measures on environment, energy, health, privatization, subsidies, taxation, natural resource management & responses to economic crises
- Political, financial, legal & social implications of awards on governance makes – this otherwise domestically disconnected – private arbitral system prone to scrutiny & criticism
- Awards contribute to *de facto* body of public international law & influence States' policies
- "Regulatory Chill" has led States to clarify, constrain & provide greater direction to tribunals

Lengthier Preambles infused with the Right to Regulate

- **CETA**
  - Preserves flexibility to achieve legitimate policy objectives (public health, safety, environment, public morals, promotion & protection of cultural diversity)
- **TPP**
  - **Inherent** right to regulate
  - Same, but adds: conservation of living/non-living exhaustible natural resources, stability of financial system
- **EUSFTA**
  - more subtle (reflected more so in standard of treatment & indirect expropriation)

Definitions: Giving Further Direction to Tribunals

- **Article 9.1 TPP** definition of 'investment' includes:

"(g) licences, authorisations, permits and similar rights conferred pursuant to the Party's law;[4]

> FN 4: Whether a particular type of licence, authorisation, permit or similar instrument (including a concession to the extent that it has the nature of such an instrument) has the characteristics of an investment **depends on** such factors as the **nature and extent of the rights that the holder has under the Party's law.** Among such instruments that do not have the characteristics of an investment are those that do not create any rights protected under the Party's law. For greater certainty, the foregoing is without prejudice to whether any asset associated with such instruments has the characteristics of an investment."

- Effects a *renvoi* to applicable local law of host State
- No equivalent provisions in CETA or EUSFTA

Substantive Provisions: Giving Further Direction to Tribunals

- Similar in many respects, but not always consistent in their approaches

- First treaties to incorporate more detailed guidance to arbitrators on:
  - (Minimum) Standard of Treatment
  - Indirect Expropriation
  - National Treatment

Minimum Standard of Treatment

- **Article 9.6 TPP**

Article 9.6: Minimum Standard of Treatment[15]

1. Each Party shall accord to covered investments treatment in accordance with applicable customary international law principles, including fair and equitable treatment and full protection and security.

2. For greater certainty, paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as the standard of treatment to be afforded to covered investments. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights. The obligations in paragraph 1 to provide:

   (a) "fair and equitable treatment" includes the obligation not to deny justice in criminal, civil or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world; and

   (b) "full protection and security" requires each Party to provide the level of police protection required under customary international law.

3. A determination that there has been a breach of another provision of this Agreement, or of a separate international agreement, does not establish that there has been a breach of this Article.

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[15] Article 9.6 (Minimum Standard of Treatment) shall be interpreted in accordance with Annex 9-A (Customary International Law).

[…]

TPP Annex 9-A

Customary International Law

Annex 9-A

Customary International Law

The Parties confirm their shared understanding that "customary international law" generally and as specifically referenced in Article 9.6 (Minimum Standard of Treatment) results from a general and consistent practice of States that they follow from a sense of legal obligation. The customary international law minimum standard of treatment of aliens refers to all customary international law principles that protect the investments of aliens.

TPP

- Narrows scope to minimum standard of treatment provided under customary international law (like NAFTA Chapter 11)

- Attempts to reign in risky provisions like ‘legitimate expectations’
  - Art. 9.6(4): “For greater certainty, the mere fact that a Party takes or fails to take an action that may be inconsistent with an investor’s expectations does not constitute a breach of this Article, even if there is loss or damage to the covered investment as a result.”
  - Legitimate expectations different than CETA (“taken into account”) & EUSFTA (legitimate expectations sufficient for finding of a breach)

EUSFTA & CETA's Closed List Approach to Minimum Standard of Treatment

EUSFTA:

Article 9.4

Standard of Treatment

1. Each Party shall accord in its territory to covered investments of the other Party fair and equitable treatment[12] and full protection and security.

2. To comply with the obligation to accord fair and equitable treatment set out in paragraph 1, neither Party shall adopt measures that constitute:

   (a) denial of justice[13] in criminal, civil and administrative proceedings;

   (b) a fundamental breach of due process;

   (c) manifestly arbitrary conduct;

   (d) harassment, coercion, abuse of power or similar bad faith conduct; or

   (e) a breach of the legitimate expectations of a covered investor arising from specific or unambiguous representations[14] from a Party so as to induce the investment and which are reasonably relied upon by the covered investor.

[12] Treatment in this Article includes treatment of covered investors which directly or indirectly interferes with the covered investors' operation, management, conduct, maintenance, use, enjoyment and sale or other disposal of their covered investments.

[13] For greater certainty, the sole fact that the covered investor's claim has been rejected, dismissed or unsuccessful does not in itself constitute a denial of justice.

[14] For greater certainty, representations made so as to induce the investments include the representations made in order to convince the investor to continue with, not to liquidate or to make subsequent investments.

Waste Management v Mexico

At para. 98:

"…**a general standard for Article 1105 is emerging**. Taken together, the *S.D. Myers*, *Mondev*, *ADF* and *Loewen* cases suggest that the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is **arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice,** or involves a **lack of due process** leading to an outcome which **offends judicial propriety**— as might be the case with a **manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process**. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant."

Indirect Expropriation: Codification of Customary International Law

- All 3 treaties reflect ***Methanex v US*** (2005) on how to distinguish between *bona fide* regulation vs indirect expropriation

"… as a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, *inter alios*, a foreign investor or investment is not deemed expropriatory and compensable **unless** specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation …"

"… the Tribunal concludes that the California ban was made for a public purpose, was non-discriminatory and was accomplished with due process … From the standpoint of international law, the California ban was a lawful regulation and not an expropriation."

TPP: Indirect Expropriation

- TPP equivalent to *Methanex* is Annex 9B(3)(b):

"Non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety and the environment, do not constitute indirect expropriations, except in **rare circumstances**."

> FN 37: "For greater certainty and without limiting the scope of this subparagraph, regulatory actions to protect public health include, among others, such measures with respect to the regulation, pricing and supply of, and reimbursement for, pharmaceuticals (including biological products), diagnostics, vaccines, medical devices, gene therapies and technologies, health-related aids and appliances and blood and blood-related products."

- All 3 FTAs similarly worded, but not identical

National Treatment

- **Art. 9.3 EUSFTA:**

"Each Party shall accord to covered investors of the other Party and to their covered investments, treatment in its territory no less favourable than the treatment it accords, **in like situations**, to its own investors and their investments with respect to the operation, management, conduct, maintenance, use, enjoyment and sale or other disposal of their investments."

TPP: National Treatment

- Art. 9.4 TPP virtually identical to NAFTA ("like circumstances")

Article 9.4: National Treatment[14]

1. Each Party shall accord to investors of another Party treatment no less favourable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory.

2. Each Party shall accord to covered investments treatment no less favourable than that it accords, in like circumstances, to investments in its territory of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.

3. For greater certainty, the treatment to be accorded by a Party under paragraphs 1 and 2 means, with respect to a regional level of government, treatment no less favourable than the most favourable treatment accorded, in like circumstances, by that regional level of government to investors, and to investments of investors, of the Party of which it forms a part.

FN 14: For greater certainty, whether treatment is accorded in "like circumstances" … depends on the **totality of the circumstances, including whether the relevant treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives**.

- *See also* (non-binding, but undoubtedly persuasive) Drafter's Note

EU Incorporates WTO-Style Exceptions Clause into National Treatment

- Art. 9.3(3) EUSFTA:

> 3. Notwithstanding paragraphs 1 and 2, a Party may adopt or enforce measures that accord to covered investors and investments of the other Party less favourable treatment than that accorded to its own investors and their investments, in like situations, subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination against the covered investors or investments of the other Party in the territory of a Party, or is a disguised restriction on covered investments, where the measures are:
>
> (a) necessary to protect public security, public morals or to maintain public order[10];
>
> (b) necessary to protect human, animal or plant life or health;
>
> (b) relating to the conservation of exhaustible natural resources if such measures are applied in conjunction with restrictions on domestic investors or investments;
>
> (c) necessary for the protection of national treasures of artistic, historic or archaeological value;
>
> (d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Chapter including those relating to:
>
> (i) the prevention of deceptive or fraudulent practices or to deal with the effects of a default on a contract;

- No equivalent provision in TPP Investment Chapter