Investor-State Dispute Settlement in the Transatlantic Trade and Investment Partnership: an Inescapable Necessity or a Trojan Horse?

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Europa-Kolleg Hamburg
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Agne Andrijauskaite*

Abstract

The main objective of this thesis is to investigate the critical arguments raised by the general public in connection with the possible inclusion of investor-State dispute settlement (ISDS) in the prospective Transatlantic Trade and Investment Partnership (TTIP) between the European Union (EU) and the United States of America and see whether they bear legal merit. In the first part, the historic origins of ISDS are traced alongside with the inquiry into the general rationale of this dispute settlement system and problems stemming therefrom, as well as the position of an ISDS in the EU’s investment architecture. The thesis then examines three main points of criticism pertinent to the ISDS-into-TTIP debate – interference with State’s right to regulate, the lack of transparency and the arbitrators’ ethics, conduct and qualifications. All of these main points of criticism are discussed on a theoretical level and subsequently the proposals how to overcome them are made. In order to get a more practical overview and envisage what exact shape ISDS might take in the TTIP, a glance at the text of Comprehensive Economic and Trade Agreement between the EU and Canada is cast and the relevant provisions are discussed accordingly. In conclusion, the thesis tries to answer to which extent is the general critique towards ISDS-into-TTIP justified and whether it is a legally tamable mechanism or should be relinquished instead.

Key words: Transatlantic Trade and Investment Partnership (TTIP), Investor-State Dispute Settlement (ISDS), Investment Arbitration, The Comprehensive Economic and Trade Agreement (CETA), Arbitration Ethics

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Agne Andrijauskaite

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# List of Abbreviations

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<td>AAA/ABA</td>
<td>American Arbitration Association and American Bar Association</td>
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<td>Arbitration Institute of SCC</td>
<td>The Arbitration Institute of Stockholm Chamber of Commerce</td>
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<td>BIT(s)</td>
<td>Bilateral Investment Treaties</td>
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<td>CETA</td>
<td>The Comprehensive Economic and Trade Agreement</td>
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<tr>
<td>Council</td>
<td>The Council of the European Union</td>
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<td>EC</td>
<td>The European Commission</td>
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<tr>
<td>ECJ</td>
<td>The European Court of Justice</td>
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<td>ECHR</td>
<td>The European Court of Human Rights</td>
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<td>EP</td>
<td>The European Parliament</td>
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<td>EU</td>
<td>The European Union</td>
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<td>FCNs</td>
<td>Friendship, Commerce and Navigation Treaties</td>
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<td>FDI</td>
<td>Foreign Direct Investment</td>
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<td>FTAs</td>
<td>Free Trade Agreements</td>
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<td>FTC</td>
<td>Free Trade Commission of the North American Free Trade Agreement</td>
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<tr>
<td>IBA</td>
<td>International Bar Association</td>
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<td>ICSID</td>
<td>The International Centre for Settlement of Investment Disputes</td>
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<td>ICJ</td>
<td>The International Court of Justice</td>
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<tr>
<td>ICC</td>
<td>The International Chamber of Commerce</td>
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<tr>
<td>ICC</td>
<td>International Court of Arbitration – The International Court of Arbitration of the International Chamber of Commerce</td>
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<td>IIA(s)</td>
<td>International Investment Agreements</td>
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<td>IIID</td>
<td>International Institute for Sustainable Development</td>
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<td>ISDS</td>
<td>Investor-State Dispute Settlement</td>
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<tr>
<td>OECD</td>
<td>The Organization for Economic Co-operation and Development</td>
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<td>NAFTA</td>
<td>The North American Free Trade Agreement</td>
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<td>NGOs</td>
<td>Non-governmental Organizations</td>
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<tr>
<td>PCA</td>
<td>The Permanent Court of Arbitration</td>
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<tr>
<td>TFEU</td>
<td>Treaty on the Functioning of the European Union</td>
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<td>TTIP</td>
<td>The Transatlantic Trade and Investment Partnership</td>
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<tr>
<td>RTA(s)</td>
<td>Regional Trade Agreement(s)</td>
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<tr>
<td>UN</td>
<td>The United Nations</td>
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<tr>
<td>UNCITRAL</td>
<td>The United Nations Commission on International Trade Law</td>
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<tr>
<td>UNCTAD</td>
<td>The United Nations Conference on Trade and Development</td>
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<tr>
<td>World Bank</td>
<td>The International Bank for Reconstruction and Development</td>
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<tr>
<td>WWII</td>
<td>The Second World War</td>
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Introduction

The United States and the European Union have been discussing a transatlantic free trade area in various guises for decades, but it was not until G8 summit in Northern Ireland on 17 June, 2013 that the formal negotiations between these two economic powerhouses on the Transatlantic Trade and Investment Partnership as a response to the global financial crisis and the collapse of the multilateral trade negotiations in the World Trade Organization (Doha Round) were launched. Negotiation groups from both sides of the Atlantic met on 8th of July, 2013 in Washington, DC for the first round of TTIP negotiations and, as of this writing, the fifth round of trade talks is scheduled to take place in Arlington, Virginia from 19th of to 23rd of May, 2014.

The comprehensive transatlantic trade agreement, once concluded, would bridge two largest world economies and is said to be capable of bringing significant economic gains as a whole for the EU (€119 billion a year) and US (€95 billion a year) and increase global income by almost €100 billion. This, in turn, translates to an extra €545 in disposable income each year for a family of 4 in the EU, on average, and €655 per family in the US.

While expected economic benefits of the prospective trade agreement look optimistic for both sides, the deal, which is mainly focusing on dismantling non-tariff barriers to trade, also known as ‘trade-irritants’, and is striving for overall regulatory coherence, was not met without obstacles and fierce opposition. The liberalization of agricultural trade, cultural services, data protection, genetically modified foods, trade-diverting effects on third countries – were only few hot-button issues regarding TTIP dispute.

Yet it is important to stress that the TTIP, as the name suggests, is not only about trade. The negotiations also covered ‘trade plus’ sectors such as public procurement and investment, the latter topic touching a public’s nerve the hardest. The possible inclusion of investor-state dispute settlement, which allows an investor to bring a case directly against a country hosting its investment, into an agreement quickly became the main bone of contention surrounding TTIP with various NGOs bashing it to be the “anti-democracy iceberg” and threatening that it will enable “to sue the living daylights out of governments”. Furthermore, the opposition became

4 Ibid.
7 The expression was coined by environmental and political activist George Monbiot.
even more galvanized with the emergence of such emblematic cases like *Vattenfall v Germany*⁸ or *Philip Morris v Australia*.⁹ Arbitral proceedings of this kind encouraged countries like Australia, Indonesia, South Africa and Ecuador to consider completely revoking its commitment to use ISDS in various BITs or FTAs. The European Commission, for its part, on 21st of January, 2014, declared a three-month reflection period on the possible inclusion of ISDS, which enabled concerned public to have its say¹⁰. What is more, due to the unprecedented controversy, Germany recently reversed its support for ISDS in the TTIP, which is believed to be a further impediment to the negotiations on investment chapter.

Such a growing public outcry and dangling fate of the ISDS-into-TTIP motivated the author of this thesis to examine this phenomenon closer and analyze whether the perceived legal perils of this mechanism such as interference with the State’s right to regulate public matters, lack of transparency and lack of independence and impartiality of arbitrators are really toxic and unsurmountable, as some critics point out. In seeking answers to these questions the historic, textual, systemic and comparative methods are employed throughout the thesis. Furthermore, the need for reform of an ISDS is also addressed and some ways how to ameliorate the system – considered. Whilst analyzing the aforesaid questions, the official position of the European Commission about investment and ISDS in EU agreements¹², the mandate given to it by the Council of the European Union for the negotiations on TTIP¹³ and the draft investment and ISDS chapter of the EU free trade agreement with Canada¹⁴ will serve as main tools. The CETA text is chosen not only because the EC has declared that the necessary improvements of the investor-State arbitration system have already been presented there and even praised it to be

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⁹ In June 2011, Philip Morris Asia Limited (based in Hong Kong) instigated arbitral proceedings under UNCITRAL against Australia claiming Australia’s plain cigarette packaging legislation is a breach of Australia’s 1993 BIT with Hong Kong. The procedural history is available at [http://www.italaw.com/cases/851](http://www.italaw.com/cases/851) (1st May 2014).


¹¹ Pertinent to the debate are substantive, as well as procedural, aspects of an ISDS system. It is oftentimes discussed what is understood under the terms ‘investment’ or ‘investor’, as well as under loosely phrased provisions like ‘fair and equitable treatment’ or ‘indirect expropriation’. Moreover, the consistency and the proliferation of frivolous lawsuits are other important points of criticism raised by the general public. Yet the author of this thesis due to its limited scope decided to choose and focus on only three aspects, which are most heatedly discussed in the general ISDS-into-TTIP discourse.


¹⁴ As of this writing (4th May 2014) the text of CETA is not publically available, yet the leaked version of the document can be found at [http://www.tradejustice.ca/leakeddocs/](http://www.tradejustice.ca/leakeddocs/) (CETA Dispute Settlement, as well as CETA Investment Texts).
‘the most progressive system of ISDS yet agreed in any agreement’\textsuperscript{15}, but also because the consultation document of the EU does not contain draft version of TTIP, but uses CETA as a reference instead. Additionally, the EU has made it clear that CETA text would be the foundation of the EU’s negotiating position with the US in relation to the investment chapter of TTIP, thus some educated guesses of what shape ISDS will take in the TTIP can be made accordingly.

1. Historic Development of an ISDS

1.1. Diplomatic protection as a precursor to the modern-day investment protection regime

“Whoever uses a citizen ill, indirectly offends the State, which is bound to protect this citizen.”

\textit{Emer de Vattel}

It is commonly argued in the literature that the investment protection regime finds its roots in the international protection of aliens abroad, the application of which gave rise to international litigation which – as is well-known – fostered the mechanism of State responsibility, first seen as a form of diplomatic protection\textsuperscript{16}. Put differently, previously the only available legal\textsuperscript{17} solution for the aggrieved foreigner at the treatment which he had received in the host State was to seek diplomatic protection from his home State\textsuperscript{18}.

Diplomatic protection is an international law mechanism through which exercise the State of an aggrieved individual makes a claim against other state for an injury to the home state’s national\textsuperscript{19}. The underlying principle of this mechanism is that an injury to a state’s national is an injury to the state itself, for which it may claim reparation from any responsible state\textsuperscript{20}. Thus, previously only state-to-state disputes\textsuperscript{21} regarding foreign investment were conceivable and individuals alongside with private non-state entities were inhibited from making individual claims against states by a fundamental lack of \textit{locus standi} under international law\textsuperscript{22}.

Yet international customary law always attached specific requirements to the exercise of diplomatic protection. Firstly, the individual seeking diplomatic protection needed to enjoy

\textsuperscript{17} The threat or use of force, also known as a ‘gun-boat diplomacy’, in regard to the investment protection overseas, was also not uncommon, yet completely outlawed by the adoption of the UN Charter and is beyond the scope of this thesis.
\textsuperscript{18} McLachlan/Shore/Weiniger, International Investment Arbitration, p. 4.
\textsuperscript{19} The well-known concept was codified in 2006 by International Law Commission, see Draft Articles on Diplomatic Protection (2006), in Official Records of the General Assembly, Sixty-first Session, Supplement No. 10 (A/61/10).
\textsuperscript{20} Newcombe/Paradell, Law and Practice of Investment Treaties: The Standards of Treatment, p. 5.
\textsuperscript{21} The most emblematic cases before ICJ concerning investment and diplomatic protection were \textit{Barcelona Traction, Light and Power Co. Ltd. (Belgium v. Spain)}, ICJ Reports 1970 and \textit{Elettronica Sicula S.p.A. (ELSI) (United States v. Italy)}), ICJ Reports 1989 in which some procedural and substantive deficiencies of diplomatic protection model were touched upon.
\textsuperscript{22} \textit{Alvik}, Contracting with Sovereignty: State Contracts and International Arbitration, p. 13.
nationality of an espousing state as a prerequisite, which in investment context would translate into a necessity of an entity to be incorporated under the laws of respective state. Secondly, an injured individual had to exhaust all local remedies available in a State hosting its investment. Finally, the use of diplomatic protection always remained a discretionary power of an injured national State and was oftentimes saturated with political or other motives because it was also a way of the respective State to shape its international relations. In other words, the interest of the investor to pursue its claim was always placed at the mercy of political discretion of its home state government. Moreover, even if the stringent criteria for exercising diplomatic protection were met, once a State decided to espouse a claim, investor would lose a control of a process and the government might have acted as it saw fit in the matter.

Given the financial interests at stake this mechanism soon proved to be ineffective and too cumbersome for investors, who were in need of legal certainty. The depoliticization of investment disputes in one form or another was thus inevitable and the use of diplomatic protection soon faded away.

1.2. Treatification as a way to overcome limitations of diplomatic protection

As noted above, the exercise of a diplomatic protection in investment context was flawed and inevitably had to move in a more politics-free direction. Thus, it was soon superseded by a ‘treatification’ process which established a brand new investment arbitration regime.

Such movement began in the 1950’s with the advent of the growth and expansion of the then new phenomenon of international investment. Various multilateral efforts, both official and non-governmental, were made to prepare multilateral conventions governing foreign investment exclusively. These included ICC’s International Code of Fair Treatment of Foreign Investment (1949), the International Convention for Mutual Protection of Private Property Rights in Foreign Countries (1957), a private effort known as Abs-Shawcross Draft Convention on Investments Abroad (1959), and the OECD Draft Convention on the Protection of Foreign Property (1967), amongst others. All these efforts failed due to the disagreement between capital exporting and capital importing states, yet they marked a paradigm change from classical protection of aliens and their property to the promotion of economic development via effective protection of investment. Besides, Abs-Shawcross Convention was the first multilateral agreement to expressis verbis include the proposition of an investor being able to directly bring a claim against a State hosting its investment. Yet it was not until Convention on the Settlement of Investment Disputes (ICSID Convention) of 1965 when such proposal fully materialized.

As noted above, all multilateral efforts to create an international framework for foreign investment failed and, as a result, capital exporting states began concluding bilateral investment

\[^{23}\text{Braun}, \text{Ausprägungen der Globalisierung: Der Investor als partielles Subjekt im Internationalen Investitionsrecht, p. 40 [Author’s translation].}\]

\[^{24}\text{Alvik (fn. 22), p. 16.}\]

\[^{25}\text{The fact that diplomatic protection has eroded in investment context was expressis verbis confirmed by the ICJ in Case Concerning Ahmadou Sadio Diallo (Republic of Guinea v Democratic Republic of the Congo), Preliminary Objections, ICJ, 24 May 2007, para 88. Moreover some legislative acts also directly renounce diplomatic protection as a suitable means of bringing international investment claim, see, for example, Art. 27 of ICSID Convention, which inter alia provides that diplomatic protection is undermined by existing arbitration agreement.}\]

\[^{26}\text{Salacuse, in: Horn (ed.), Arbitrating Foreign Investment Disputes, p. 55.}\]

\[^{27}\text{Ibid., p. 56.}\]
treaties (BITs) dedicated to foreign investment promotion and protection. It is an uncontested fact that exactly those repeated failures to make investment protection part of multilateral regime triggered a general move towards bilateral treatification. It is also said that Friendship, Commerce and Navigation Treaties (FCNs), which the European colonial powers and the US have been concluding for a long time, were antecedents of BITs, however, they mainly focused upon the trade and navigation with investment protection clauses being incidental. The modern day creation of global BITs, which dealt exclusively with foreign investment, network, for its part, was triggered by Germany. Having lost its foreign investment as a result of its defeat in the WWII, it was especially sensitive to the political risks to which foreign investment was exposed and concluded the first two BITs, one with Pakistan and the other with the Dominican Republic in 1959. Other individual European countries quickly followed suit and started concluding various BITs with a broad array of developing countries. Encouraged by the experience of the Europeans, the US in 1981 launched its own programme to negotiate specific BITs with other countries.

Nonetheless, it was not until the late 1980’s when a true expansion of BITs’ network influenced by the fall of Berlin Wall and the increasing endorsement of economically liberal policies took place. Such network of BITs was judicialized with the more systemic inclusions of investor-State arbitration and the first investor-State type of dispute under BIT was registered in 1987. An avenue for investors to directly defend their rights under applicable agreements without having to rely on the diplomatic protection mechanism was thus fully solidified and the BITs continue to mushroom up to this day. While in 1989 there were 385 BITs, currently we can count 2,857 BITs and 339 other IIAs, such as integration or cooperation agreements with an investment dimension. This seems to be a huge number at a first blush, yet UNCTAD points out that in order for all members of the UN to be covered by a BIT with all other members, over 18,000 treaties would be required. From the category of regional agreements NAFTA and the Energy Charter Treaty, which authorize compulsory investment arbitration, are worth to be highlighted. Most of these treaties provide for ICSID arbitral settlement of investor-State disputes, while some opt for Arbitration Rules of UNCITRAL or other forms of arbitration.

With the proliferation of various IIAs investment arbitration exploded as well. First dispute, as mentioned above, was registered in the late 1980’s, however, it was not until 1996 that, in the words of one ICSID staff member, ‘the floodgates…seemed to open’. Today there are 568 known treaty-based cases and 98 States have been respondents. In the end of 2013 alone at least 57 known ISDS cases pursuant to IIAs were initiated which comes close to

28 Newcombe/Paradell (fn. 20), p. 41.
29 D’Aspremont (fn. 16), p. 18.
31 Salacuse (fn. 26), p. 58.
32 D’Aspremont (fn. 16), p. 18.
previous year’s record high number of new claims\textsuperscript{38}. What is more, today international arbitration is even encouraged in the Guidelines on the Treatment of Foreign Direct Investment promulgated by the World Bank in 1992. Even though these Guidelines are not legally binding, they do reflect an international trend of many states to provide for arbitration of disputes with nationals of other states either through direct agreement with those nationals or in BITs or investment laws\textsuperscript{39}.

1. 3. ISDS in the EU’s investment architecture – newly gained competence and a push forward

The development of EU’s common investment policy is a relatively new phenomenon. Since 2000 the EC has become increasingly concerned over the fact that various BITs Member States have concluded may distort the internal market, with each state seeking its own advantage rather than adhering to common rules\textsuperscript{40}. However, it was not until 2009 when the ECJ expressly declared\textsuperscript{41} that certain provisions are incompatible with EU law, thus highlighting that the existing legal framework has to be established\textsuperscript{42}. The EC in response to this jurisprudential development announced its resolve to establish a new EU investment policy\textsuperscript{43}. Adoption of the Lisbon Treaty, for its part, introduced Article 207 TFEU, which endowed the EU with the exclusive competence over FDI.

In its salient document on the future of European investment policy, EC presented ISDS as “forming a key part of the inheritance that the Union receives from Member State BITs”\textsuperscript{44}. The Council in the inter-institutional dialogue that began\textsuperscript{45} agreed with the EC’s approach, whilst stressing “the need for an effective investor-to-state dispute settlement mechanism in the EU investment agreements”\textsuperscript{46}. The EP, even though voicing some criticism and calling for a reform of an ISDS, also took the view that “in addition to state-to-state dispute settlement procedures, investor-state procedures must also be applicable in order to secure comprehensive investment protection”\textsuperscript{47}. The EC subsequently agreed to points of critique raised by the EP and, thus, the overall approach to the ISDS was the one of ‘endorsement and fine-tuning’: ISDS was not excluded from criticism, but in principle was considered to be important and desirable\textsuperscript{48}.

\textsuperscript{38} Ibid.
\textsuperscript{39} Comeaux/Kinsella, Protecting Foreign Investment under International Law: Legal Aspects of Political Risk, p.186.
\textsuperscript{40} De Mestral, in: De Mestral/Lévasque (eds.), Improving International Investment Agreements, p. 43;
\textsuperscript{44} Ibid, p. 9.
\textsuperscript{48} Tams (fn. 46), p. 7.
The leaked drafts of CETA and TTIP, however, marked the twist in the debate and the generally positive approach towards ISDS now seems to be in flux. This was clearly exemplified not only by the aforementioned EC’s decision to consult the public on the possible inclusion of ISDS into TTIP, but also by the latest EP remonstrations whilst debating the EC’s proposal for a framework for allocating financial responsibility for ISDS awards. The EP in regard to this proposal adopted a series of amendments at odds with both the Council and the EC, inter alia noting that future treaties should afford “no higher level of protection than Union law and the general principles common to the laws of the Member States granted to investors from within the Union”.

Needless to say, the EU is a long way from a coherent investment policy because of the divergent Member States’ views on the system and other pertinent problems, such as the fate of intra-EU BITs, which fall outside the scope of this thesis. Likewise, the ultimate position of an ISDS in the EU’s investment architecture or the form it will acquire remain unclear, although some educated guesses drawn from the reference to CETA may be made. However, a pattern of the EC to be pushing ISDS forward cannot go unnoticed and requires couple of remarks relevant to this thesis.

Firstly, it is said that the incorporation of provision of ISDS in the TTIP would set a ‘golden standard’, which in turn can be beneficial in the EU’s negotiations with India or China on investment chapters. This endeavour, in the author’s view, can be best analogized with the US and Canada successfully drawing Mexico into the orbit of ISDS via NAFTA. The US and Canada already had a mutual trade agreement in place, but in seeking to include investment protection and bring Mexico into the arrangement, they were forced to add ISDS in order to deal with what were perceived to be concerns about the Mexican courts. Clearly, having a properly functioning ISDS established in the EU-US area, which accounts for roughly a half of global FDI outflows, would be hard to ignore and circumvent in any kind of future negotiations.

Secondly, the EC is eager to make use of an ISDS because of a newly gained treaty-making competence. Assuming that the EC is a rational actor, it is quite plausible that it wants to show results in its new role and secure its position in the field previously dominated by the ministries of Member States. This proposition is substantiated by EC’s inclination to understand its competence in investment field extensively, i.e. in a way to include not only FDI, but also portfolio investment, of which Article 207 TFEU makes no explicit mention, by using implied powers doctrine. However, even though EC seems intent to assert its broad new investment

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51 Member States have different experience dealing with ISDS. For example, Czech Republic was sued under this mechanism dozens of times, while Ireland has concluded only one BIT overall. Therefore, the concerns raised by them differ, as do the interests different Member States bring to the bargaining table.
52 It is not clear whether EU will adopt UNCITRAL or other arbitration rules for its model ISDS. The possibility of the EU adhering to the ICSID Convention, for its part, remains foreclosed because it is open only to member states of a World Bank or to any other state which is party to the ICJ Statute (ICSID Convention, Art. 67).
powers as a matter of principle, it is struggling to provide content to its exercise. This will have to be rectified in the future and this task will be uphill.

2. General rationale of an ISDS and problems attached thereto

2.1. The emergence of a brand new *locus standi* for investors in their quest for a neutral dispute resolution forum

“There is little use in going to law with the devil while the court is held in hell.”

*Humphrey O’Sullivan*

As stated in the previous chapter, the exercise of diplomatic protection proved to be deficient in the context of investment and was replaced by the proliferation of investment treaties, which granted direct access to arbitration for foreign investors. The creation of an ISDS, as a counterweight, marked a revolutionary step in the eyes of international law and modified the classical notion that only states have the capacity to bring claims before international judicial bodies directly.

While 30 years ago a foreign investor might only have had a slim chance of making use of diplomatic protection, it could now be in a position to pursue such a claim directly, without the assistance or approval of its state of nationality. In other words, investors by pursuing their own economic agenda became their own “private attorney general” or ISDS allowed “the true complainant to face the true defendant.” The right to international adjudication of investors was undoubtedly a groundbreaking procedural benefit and was even termed to be as “one of the most important progressive development in the procedure of international law of the twentieth century.”

Such emergence of a full-blown *locus standi* and partial international legal personality can be derived from investors’ search for a neutral legal forum. Diplomatic protection was too cumbersome for investors, but they were also unwilling to litigate in national courts of a host State by themselves. The prime reason for such reluctance lies in the fact that historically ISDS has been included in investment agreements with developing countries, which did not enjoy high level of rule of law and was designed to provide investment with a remedy it would otherwise lack. Developing countries were inclined to accept this investor *qua* State mechanism due to the fact that most of their BITs were concluded in a short period after the governments adopted a liberal policy and it was crucial for them to encourage foreign investment and commit to a high level of investor protection. Those countries with less to offer in terms of their

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59 This pattern remains relevant also today – ISDS is planning to be included into EU-Myanmar Bilateral Investment Treaty with the rationale that foreign investors cannot find relief in domestic courts of a country that has been closed to a democratic world for many years.
60 Van Harten, Investment Treaty Arbitration and Public Law, p. 41.
domestic market, resources or workforce were compensating by giving up more legal rights to investors, or, put it differently, were ‘bidding up’ for international capital. Thus, it can be claimed that this mechanism was designed to reduce a legal risk premium while investing in developing countries.

In addition to that, investors not only worried that national courts can be corrupt or unreliable or serve as instrumentalities of the host government as such. It is generally agreed that even the most impartial national court may be more deferential and show greater understanding for the concerns of its home government than a neutral and detached international judge or arbitrator would. This phenomenon is sometimes called inherent national prejudice since judges are drawn from certain nationalities. In order to overcome the lack of confidence in the host country’s judiciary and to prevent the propensity to favour government’s position a neutral dispute resolution fora had to be invented. The ultimate goal of an ISDS can be thus summarized as “setting the parties on equal footing in terms of avoiding breach of contract and, failing that, providing for a neutral resolution of any disputes.”

2.2. ISDS – an unhappy marriage between international commercial arbitration and public law?

It can be inferred from the previous chapter, that ISDS inter alia was borne out of the search for a neutral dispute resolution forum. Such perceived neutrality of arbitral forum per se is nothing new and was used in international commercial arbitration for centuries in order to cater for international business needs. Yet in investment context it raises certain conceptual problems.

It must be noted that in international commercial arbitration circumventing national courts is not considered to be problematic because arbitrator’s power and jurisdiction derive from the intention of the parties as expressed in the contractual relationship. This party autonomy, as an integral part of a general freedom of contract, encompasses the ability to choose substantive, as well as procedural law. As such, the arbitration proceedings are viewed as an expression of the will of the parties. In investment arbitration, though, such contractual relationship for a foreign investor, acting as a claimant, with a State, is non-existent, but instead it is replaced by a general State’s ex nunc consent to arbitration given for indeterminate class of claimants in, for example, respective BIT, earning the whole process a label of an ‘arbitration without privity.’ Besides, in investment context dispute arises not between two juridical equals, but between a private actor and a State, which possesses regulatory domain. Thus, international

61 Ibid., p. 41-43.
62 Horn, in: Horn (ed.), Arbitrating Foreign Investment Disputes, p. 28.
63 Alvik (fn. 22), p. 44.
64 Lew/Mistelis/Kröll, Comparative International Commercial Arbitration, p. 5.
65 The search for such a neutral forum is expressis verbis reflected in Art. 1115 of NAFTA, delimitating the purpose of ISDS and claiming that such mechanism “assures both equal treatment <…> and due process before an impartial tribunal”.
68 Ibid.
69 Such description to ISDS was given by Jan Paulsson in his ground-breaking article, see, Paulsson, ICSID Review – Foreign Investment Law Journal 1995 (Vol. 10, No. 2).
investment arbitration elevates judicial review of a State’s conduct to a new level and can even be compared to a ‘species of a global administrative law’\(^{70}\) or ‘efflorescent field of global administrative law’\(^{71}\).

Despite the aforementioned public law character of investment treaty arbitration, the procedure it uses follows the model of international commercial arbitration\(^{72}\). Moreover, apart from applying the procedural framework, international investment arbitration also uses the enforcement structure of international commercial arbitration by incorporating ICSID Convention and the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 (New York Convention) into the system. It is also noteworthy that international commercial arbitration is based not only on neutrality of arbitral forum, but also on the perceived benefits of flexibility and confidentiality, amongst others. These preconditions allow disputing parties to escape the rigidity of formal litigation and tailor the proceedings in a way which suits particular needs of a dispute the most and also to keep commercial secrets away from the publicity. However, these advantages of commercial arbitration do not appear to be suitable in a dispute where regulatory powers of a State are challenged because legal relationship is asymmetric. In other words, the heart of the problem lies in the fact that investment treaty arbitration transplants private adjudicative model from commercial sphere into the realm of public law, thereby charging privately-contracted arbitrators with the authority to make what are in essence governmental decisions\(^{73}\).

Such piggybacking of investment arbitration on rules carved out for settling cross-border business disputes seems to undermine the legitimacy of the whole system in the public’s eye because elements of ‘private justice’ are transplanted into a public realm.

2. 3. The lack of public debate around nascent ISDS and the cost of having to bear \textit{fait accompli}

As mentioned previously, ISDS is nothing new on the international plane, yet only with the launch of CETA negotiations critical voices started to emerge and with the start of TTIP talks – they became the loudest. Such enhanced scrutiny, in the author’s view, is attributable not only to the sheer scale of both agreements, but also to the lack of public debate when ISDS was \textit{in statu nascendi}.

Firstly, there was little, if any, public debate on the consequences of the US having to respond to claims under investment treaties until 15 years after the US Administration adopted its BIT programme\(^{74}\). Likewise, in Western Europe, a public debate on investment treaties took place only after a draft of the OECD’s Multilateral Agreement on Investment was leaked to and distributed by NGOs, and this was 25 years after the region’s early BITs were concluded\(^{75}\).

Secondly, little debate was had on the implications of using the commercial model to resolve claims arising out of investment treaties for violations of international legal principles whilst

\(^{70}\) Van Harten/Loughlin (fn. 36).
\(^{73}\) Van Harten/Loughlin (fn. 36), p. 126.
\(^{74}\) Van Harten/Loughlin (fn. 36), p. 126.
\(^{75}\) Ibid.
negotiating salient ICSID Convention\textsuperscript{76}. Quite the contrary – the drafters of ICSID Convention saw using ISDS mechanism primarily for contract disputes with States, a natural progression of commercial arbitration techniques\textsuperscript{77}. Finally, the Treaty of Lisbon inserted FDI into the existing framework of a broadened EU’s Common Commercial Policy also without much public debate\textsuperscript{78}.

Not only any noticeable debate of using modern form of ISDS was missing, but there was also little public outcry about States having to pay arbitral awards in favour of investors over the past few decades. Such lack of fundamental public debate precluded the possibility to reform ISDS. It was not until 2010 when dozens of academics wrote a public statement addressing the various drawbacks of international investment regime and recommended to review it\textsuperscript{79}, whereas the more profound UNCTAD paper calling for reforms appeared in 2013 only\textsuperscript{80}.

Thus, the general public seemed to have found itself confronted with a \textit{fait accompli}, rather than with an evolving legal novelty they could contribute to. Such perception that the current system of investment protection (with ISDS as an essential component) was devised without serious public debate – only to be presented as a “key part of the inheritance”\textsuperscript{81} generated a lot of anxieties and a sense of exclusion. These sentiments, however, whilst raising valid concerns, fail to have legal merit for most part as it will be shown below. Therefore, a 3 month reflection period, in the author’s view, is a positive step, which can partly make up for an abstinence of a wider discussion and inject new ideas how to improve the system from various stakeholders.

\section{ISDS-into-TTIP: Main points of critique and can they be countered?}

\subsection{ISDS and its interference with the State’s right to regulate public matters}

“I’ve seen the letters from the New York and DC law firms coming up to the Canadian government on virtually every new environmental regulation <…>. Virtually all of the new initiatives were targeted and most of them never saw the light of day.”

\textit{Former Canadian government official}

Apart from general problems, attributable to the very nature and genesis of a modern ISDS, there are specific problems surrounding possible inclusion of ISDS-into-TTIP, which seem to electrify general public. One of the main specific problems is oftentimes times characterized as a regulatory ‘chilling effect’, which describes a shrinking of domestic policy space as an outcome of skyrocketing\textsuperscript{82} arbitral awards.

\textsuperscript{76} Clodfelter (fn. 53), p. 172.
\textsuperscript{77} Ibid.
\textsuperscript{78} Reinisch, Santa Clara J Int'l L 2014 (Vol. 12, No. 1), p. 114.
\textsuperscript{81} Tams (fn. 46), p. 10.
\textsuperscript{82} The biggest known arbitral award was made in a case \textit{Occidental v. Ecuador}, in which ICSID tribunal ruled that the Republic of Ecuador has breached the US-Ecuador BIT and was ordered to pay 2.3 billion US dollars (with an
It is intrinsic to the prerogative of public power and democratic majority rule that every government must enjoy a large measure of freedom to form policies according to the changing circumstances and its own current priorities. Such authority to provide for the public health, safety and morals is sometimes called the police power of a State. However, losing a case in investment arbitration or having to pay huge compensations to investors as an outcome of regulatory measures, which are declared to violate substantive investment protection norms, or even the mere threat of expensive lawsuits can dissuade governments from enacting certain legal measures. Such possibility of governments abandoning or watering down laws in favour of investment protection seems to be one of the major concerns circulating in the whole ISDS-into-TTIP debate, since human rights in the area of labour, safety, social security and environmental law are “especially sensitive to violations by foreign investors”.

However, the bogeyman of a shrinking domestic policy space must be whisked away. Firstly, there is a dearth of evidence in relation to the effect of protections afforded to investors on the adoption of regulatory measures. Quite the opposite – in the absence of specific evidence to the contrary it is likely that most decision makers do not internalize the limits of protections offered by IIAs when evaluating the adoption of new governmental measures. Moreover, in the author’s view, the true ‘chilling effect’ can only take place in the situations, which are identical or very similar to the ones already ruled upon or pending arbitration. An example for it can be the announcement of the New Zealand’s Government to postpone legislation plans of ‘plain packaging’ until the final outcome of investment proceedings against Australia on the same matter. However, investment arbitration is one of the fastest-developing area in international law and it is hard to predict which governmental measures will be challenged and declared to be violating substantive investment protection provisions, which tend to be formulated in vague terms, next. Additionally it must be said that since no doctrine of precedent (in the sense of stare decisis) exists in investment arbitration, the ‘chilling effect’ can only be deemed to be political, but not a legal effect. This argument is further underpinned by the fact that international tribunals do not possess an authority to nullify laws. Put differently, international investment arbitration cannot be equated to constitutional or administrative judicial review for the tribunals are not able to order to repeal the measure. Therefore, the States even in the event of having to pay arbitral awards can formally uphold contested legislation.

Secondly, there are ways how to accommodate this popular fear of investment provisions being able to kill regulations and balance State’s regulatory space with foreign investors’ protection or, put eloquently, to reintroduce the ‘S’ word into the realm of investment.

interest applied), see Occidental Petroleum Corporation v. The Republic of Ecuador, Award, ICSID Case No. ARB/06/11 (Oct. 5, 2012).

Alvik (fn. 22), p. 274.


Meckenstock, Investment Protection and Human Rights Regulation: Two Aims in a Relationship of Solvable Tension, p. 99.


Ibid.


It is noteworthy, that there is an expanding tendency to include special provisions aimed at declaring that the investment promotion and liberalization objectives of international investment agreements must not be pursued at the expense of other key public policy objectives. For example, this tendency is implemented in a modified US model BIT template of 2004, which expressis verbis provides that it is inappropriate to encourage investment by weakening or reducing the protections afforded in domestic environmental law or in domestic labor laws. Such clause safeguards the flexibility of the US to regulate matters of public concern. Another example could be the Article 25 of IISD’s Model International Agreement on Investment for Sustainable Development, which inter alia embeds the right of States to pursue their own development goals and objectives and related social, economic and other policy goals. Moreover, for the first time ever the mandate for the inclusion of such ‘right to regulate’ clause, proposed and strongly defended by Belgium, was given to the EC concerning negotiations with Canada, India and Singapore. This trend of including such general exception clauses is said to codify the already existing arbitral jurisprudence, which recognizes regulatory flexibility to host States in pursuing the specific legitimate objectives. In the author’s view, the inclusion of an express provision clarifying that fostering of investment goals may not be pursued at the expense of other key public policy objectives into TTIP would also be beneficial. The practical ways of doing it are examined in a subsequent chapter.

3.1.1. Proposals how to reconcile State’s right to regulate with an effective investment protection

For reasons set out above, the inclusion of an explicit article, the so-called ‘escape clause’ or ‘police power exception’, which asserts the inherent State’s right to regulate matters of public importance could be an essential tool in pacifying the tension between this right and the goal of protecting investment. However, such article should not be the mere legal tautology, i.e. it should not purely reaffirm that a state is entitled to do what is not prohibited to do anyways, but rather shine the interpretative light for the adjudicators on the eventual application of a respective IIA. Such escape clauses could be drafted in a broad or narrow manner. They could also be telos-based (enumerating various governmental aims such as public health, safety, environment, etc), area of law focused (stating that domestic regulation in certain areas of law such as human rights, public health, safety or environmental law are exempted) or situation-based (providing that regulatory measures are exempted from the triggering of compensatory duties if certain situation is present). The exact formulation of such clause is a matter of a legislative technique.

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97 Meckenstock (fn. 85), pp. 127 – 129.
Nonetheless, the author of this thesis believes that in the TTIP context the clause should be tailored in a way that its *ratione materiae* covers the spectrum of the voiced and plausible concerns attributed to the investor-state arbitration with the environmental protection and public health standing at the fore. The list of protection-worthy areas should in no way be *numerus clausus*, but rather formulated flexibly, i.e. leaving enough room for the unanticipated contingencies the ever-changing economic reality might bring.

### 3.1.1.1. The inclusion of deferential standards of review as an interpretative tool

In order to charge an escape clause with interpretative power, the incorporation of the deferential standards of review could be sensible and help to delineate individual rights of investors and rights of sovereign States to limit such rights. Arbitral tribunals could use concepts recognized by public law in various international and national courts and tribunals, primarily by having recourse to proportionality analysis in order to reconcile rights and rights-limiting policy choices. Proportionality is a concept very well worked out in the EU, but also recognized in the US common law with its *ratio legis* being to maintain a balance between the interests of the public and those of the individual. A proportionality methodology would provide a structured analysis about the relationship between the investor’s expectations and competing public interests in the application of rule of law standards and the balance between the two. Thus, the inclusion of this requirement into an escape clause, emphasizing that regulatory measures of a State conducted in a proportionate manner should not be deemed to violate IIA, could prove to be instrumental in solving the aforementioned tension.

Another possible standard of review worthy to be included into an escape clause is *bona fides* or good faith requirement. The good faith principle is undoubtedly a recognized fundamental norm in many domestic and international contexts or, as ruled by ICSID in *Mobil Corporation et al. v Venezuela*, which conducted a comparative analysis on the misuse of law, the principle of good faith is accepted by all legal orders. This standard requires weighing and balancing irreconcilable interests. Two basic elements are pertinent thereto: first, the state has to be engaged in honest and fair dealing, and, secondly, there has to be a justification for the assertion of the escape clause provision. Where evidence exists that a state invokes its interests, perhaps through an escape clause, just as a pretext for ulterior economic motives, or where the connection between the measures taken and national security is as spurious as to clearly breach the good faith requirement, a conclusion that good faith standard was not satisfied could be reached. Thus, good faith requirement acts as a shield from opportunistic behaviour

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99 *Engle*, DLJ 2012 (No. 10), pp. 7 – 8.
101 *Kingsbury/Schill* (fn. 98), p. 103.
103 *Mobil Corporation, Venezuela Holding et al. v Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/27, Decision on Jurisdiction, 19 June 2010, para 169 – 185 // The good faith requirement is further entrenched in such a salient case as *Saluka Investments B.V. v The Czech Republic* where tribunal has expressly held that States are not liable to pay compensation to a foreign investor when they adopt in a non-discriminatory manner *bona fide* regulations that are aimed at the general welfare, see, *Saluka Investments B.V. v The Czech Republic*, UNCITRAL, Partial Award on Jurisdiction and Liability, 17 March 2006, para 255.
105 Ibid.
of the State. However, the good faith is oftentimes characterized as being too nebulous, i.e. hard to define, therefore an extra caution must be exercised whilst enshrining this deferential standard of review. Clearly, this standard alone will not be a magic formula capable of delineating the border between investment protection and regulations aimed at the general welfare of a State efficiently.

Finally, an inclusion of margin of appreciation into an escape clause could be contemplated. Margin of appreciation is a doctrine primarily developed by the ECtHR and is based on the idea that international courts should grant national authorities a certain degree of deference and respect their discretion in a way they fulfill their international law obligations\textsuperscript{106}. Thus, incorporating margin of appreciation, as a standard of review, would grant an appropriate amount of latitude to national authorities undertaking public rights while still taking into consideration investors’ rights. Moreover, it would promote legitimacy, and perhaps even accountability, by returning national authorities to the center of decision-making and placing the \textit{ad hoc} arbitral tribunal, with less connections to the domestic polity and potentially not so much expertise, in the more limited supervisory position\textsuperscript{107}. Despite the perceived benefits of including margin of appreciation standard into an escape clause, the fact that there is a polarized academic debate surrounding this standard bears noting\textsuperscript{108}. The main critique of it is revolving around the fact that the margin of appreciation is a legally hollow concept providing no exact scope or degree of deference. It is rather left for the adjudicators to work out the concrete content of the standard on a case-by-case basis, which in investment context can lead to interpretative cacophony since it lacks unified judicial body.

3. 1. 1. 2. The expansion of epistemic communities as another means to solve the tension

The list of possible deferential standards of review set out above is in no way exhaustive and is \textit{per se} not the only solution how to reconcile investment protection with State’s regulatory actions in the interest of citizenry. As already noted, investment arbitration is piggybacking on international commercial arbitration and investment-treaty arbitrators tend to come from the private law background. Moreover, it is known that the community of these arbitrators is very tightly-knit and homogeneous with solid links to corporate world\textsuperscript{109}. Bearing in mind that the vertical structure of investment arbitration distinguishes it from commercial arbitration, private law background of arbitrators does not seem to be very suitable.

The problem of such homogeneity and perceived pro-business bias could be tackled by making a roster of arbitrators more diversified, i.e. including more lawyers with public law background therein\textsuperscript{110}. Such expansion of epistemic communities – one coming from the field of commercial law and arbitration and the other coming from public international law and inter-State dispute – would be helpful in solving issues of factually and legally complicated nature.

\textsuperscript{106} Shany, EJIL 2006 (Vol. 16, No. 5), p. 910.
\textsuperscript{107} Burke-White/Von Staden (fn. 104), p. 719.
Not only would it diversify decision-making, but also potentially counterbalance groupthink, which is a known phenomenon occurring amongst people who share the same background and *esprit de corps*\(^{111}\). Both groups could contribute specific expertise to international investment law and investor-state dispute resolution: knowledge of international law and expertise with regard to international relations and dispute settlement involving sovereigns in the case of public international lawyers; a comprehension of international business transactions and business practices; and close familiarity with arbitral procedure, including know-how in complicated fact-finding, in the case of commercial arbitration practitioners\(^{112}\).

Furthermore, an arbitrator from a country whose policy is being reviewed can be added to the panel, despite the fact that in arbitration world there is an unstated presumption that being a national of a party indicates partiality or lack of independence or both\(^{113}\). It is noteworthy, that most (but not all) international tribunals\(^{114}\) called upon to engage in public law adjudication have ties that ground the tribunal in the norms and values of the state whose policies are being considered\(^{115}\). States are likely to respect and perhaps even obey such arbitrators because of their understandings of social and political context and their ability to transfer that understanding in their opinions\(^{116}\). In other words, nationality as a factor in adjudicating public law disputes provides some psychic ‘ownership’ to the States\(^{117}\). Similarly, where decisions must be accepted by national governments and their polities, those judges must understand the political and social contexts of their decisions\(^{118}\).

Such practice of permitting shared nationality between arbitrator and the State involved in arbitration, despite the aforementioned presumption, can be found in Article 13(5) of ICC Arbitration Rules and is not considered to be in conflict with impartiality or independence of arbitrators. However, taking into account that the whole system of modern investment arbitration was borne out of search for depoliticized and law-bound fora, transcending national courts, this initiative should be exercised with a particular caution. It is important not to frustrate system’s initial goals and not to make it procedurally tilted in favour of a State, which is acting as respondent. Finally, the appointed national judges should not be turned into what Jan Paulsson calls ‘a species of advocate’\(^{119}\). The excessive judicialization of a neutral dispute resolution forum could quickly turn out to be detrimental.

### 3.1.2. A glimpse into TTIP and CETA negotiations: is the fear of shrinking domestic policy space justified?

\(^{111}\) The concept of a groupthink was introduced by Irving Janis in his famous book, see, *Janis*, Victims of Groupthink: A Psychological Study of Foreign-Policy Decisions and Fiascoes.

\(^{112}\) *Schill*, in: *Schill* (ed.), International Investment Law and Comparative Public Law, p. 12.


\(^{114}\) The ICJ and the ECJ include a judge from a litigating State, whilst African Court on Human and People’s Rights *expressis verbis* prevent national judges from hearing respective cases.

\(^{115}\) *Burke-White/Von Staden* (fn. 104), p. 713.

\(^{116}\) *Ibid*.


\(^{118}\) *Ibid*.

After having considered theoretical proposals how a State’s right to regulate public matters could be reconciled with investment protection, it is worthy to cast a look at the TTIP and CETA negotiations and see whether any of them were implemented.

In its official fact sheet and public consultation on modalities for investment protection and ISDS in TTIP document the EC declares its intent to improve ISDS system in two-fold ways: firstly, by clarifying and improving investment protection rules (substantive dimension) and, secondly, by improving how dispute settlement system operates (procedural dimension). It identifies the possibility of using current investment protection rules in a way to prevent States from making legitimate policy choices as a main concern and reaffirms the right of the States to regulate in order to pursue legitimate public policy objectives. The recent mandate given by the Council to the EC for the TTIP negotiations, for its part, also reiterates that investment protection should be without prejudice to such right. It can be inferred from the aforementioned documents that the EC strives to prevent this inherent right from being undermined by tailoring substantive investment protection provisions in a clear and precise way. Namely – according to the position of the EC, ‘indirect expropriation’ and ‘fair and equitable treatment’ are two in traditional BITs vaguely formulated standards that most frequently are used by investors to make frivolous lawsuits against the States. Thus, in the present context they require clarifications and limitations which can serve as interpretative guidance. The EC goes on to state that all EU’s FTAs will preserve the principle that States are free to regulate in order to pursue legitimate public policy objectives and that EC has already introduced these improvements to the CETA.

It becomes apparent from the leaked version of CETA that both signatories in fact recognized the right of States to take measures to achieve legitimate public policy objectives not only in the preamble of the whole document, but they also agreed to include a general exception clause (Article X: General Exceptions), enabling States to adopt and enforce measures directed to public policy aims, even though this clause might not be applicable to expropriation and fair and equitable treatment standards (according to the proposal of the EU) and its ultimate content is still pending. While Canada, inspired by its new model BIT language, is willing to incorporate only three categories of measures – those, which protect human, animal or plant life or health – EU has much more expansive approach in this regard and is additionally willing to incorporate public security, public morals and public, as well as national treasures of artistic, historic and archaeological value. Moreover, Article X para 1 (b) makes it clear that two standards of review [of a measure] are attached thereto, namely – it states that the public policy measure: (i) should not be applied in a manner that constitutes arbitrary or unjustifiable discrimination between investments or between investors or (ii) it should not be a disguised restriction on international investment. In the author’s view, the inclusion of separate escape clause with a broad bundle of sectorial areas protecting public goods in the CETA text is a commendable achievement, however, the further inclusion of the above-mentioned deferential standards of review, especially the proportionality requirement in order to balance the tension between two rival rights even more, could be contemplated in the TTIP.

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120 European Commission, Fact Sheet (fn. 12).
121 European Commission, Public consultation on modalities for investment protection and ISDS in TTIP (fn. 12).
122 Council of the European Union (fn. 13).
It is also noteworthy to stress that the EU in the CETA text does not confine itself to general escape clause, but is also striving to include various horizontal exceptions. Such horizontal exceptions incorporated in the non-discrimination provisions concerning environmental protection, consumer protection or health and are designed to justify differences in treatment between investors and investments where necessary to achieve public policy objectives. Furthermore, a non-preclusion provision for taking measures for prudential reasons, including the ones granting financial stability, is foreseen and special exceptions applying in the situation of crisis, such as in circumstances of serious difficulties for the operation of the exchange rate policy or monetary policy, balance of payments or external financial difficulties, or threat thereof. Such measures, in the author’s view, can be seen as a direct repercussion of recent claims arising from crisis-related and financial austerity measures. The addition of these horizontal safeguards is another welcome development, capable of dealing with specific situations and providing more clarity thereof.

A closer look at the CETA text also reveals that the expropriation and fair and equitable treatment standards are clarified as intended, although, according to EU’s proposal they should also be eliminated from the scope of application of Article X: General Exceptions. Firstly, Paragraph 3 of the Annex to the Expropriation clause provides that non-discriminatory measures (unless they are manifestly excessive in light of their purpose) taken to protect public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations. Secondly, the fair and equitable treatment standard in Article X.9 is set out as a closed list of basic rights for investors (paragraph 2) in addition to the provision that breach of this standard may occur by treatment which is contrary to what is accepted as law in the general practice of States (paragraph 3). Moreover, there is also a requirement for the Parties to regularly or upon request review the content of this standard (paragraph), which is a paragon of the so-called evolutionary clause, which enables signatories of the treaty to deal with the changing conditions ex post. In the author’s view, in comparison to the investment protection standards found in modern BITs, which for the most part are drafted on a model contemplated in the 60’s, these clarifications reflect a clear improvement. By making previously loosely worded standards more determinate, treaty drafters leave less leeway for adjudicators to interpret the content of such standards freely.

From the analysis of substantive improvements described above, it is safe to conclude that the EU is striving for effective reconciliation of States rights to regulate with investors’ interests by including express clauses and clarifying crucial investment protection standards. However, it is not using the public law instruments to their fullest potential and further inclusion of deferential standards could be contemplated.

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125 These measures concern not only investment protection, but investment liberalization as well, for example, Article X.4 2 (d) (Market Access) provides that measures seeking to ensure the conservation and protection of natural resources and the environment are not considered to be inadmissible limitations on market access.

126 For example a special [numberless, p. 22 of CETA Investment Chapter, fn. 123] paragraph on Balance-of-Payments Exceptions provides that States have a right to adopt and maintain restrictive measures that restrict transfers of where the Party experiences serious balance-of-payments difficulties and external financial difficulties or the threat thereof.<...>.

127 In 2012 a number of investment cases emerged that have their origin in the recent financial crisis and the economic recession and in 2013 two of the cases relating to the Greek financial crisis were brought // UNCTAD (fn. 37), p. 5 and UNCTAD, Recent Developments in Investor-State Dispute Settlement (ISDS), May 2013, available at http://unctad.org/en/PublicationsLibrary/webdiaepch2013d3_en.pdf (12th May 2014).

128 The proposal of adding arbitrator of a same nationality as the State hosting investment to the panel or expanding the epistemic communities will be examined more closely in a chapter dealing with improvements of arbitral corps.
3. 2. The lack of transparency

“Our meetings are secret. Their members are generally unknown. The decisions they reach need not be fully disclosed. Yet the way a small group of international tribunals handles disputes between investors and foreign governments has led to national laws being revoked, justice systems questioned and environmental regulations challenged.”

Anthony de Palma

Another issue surrounding ISDS, revamped by its possible inclusion into TTIP, is that it is being held out of the public’s eye. Such lack of transparency, for its part, can be understood in two-fold ways: one pertinent to the modus operandi of ISDS, another – to secrecy and deficit of public involvement concerning TTIP negotiations. The latter falls outside the scope of this thesis because the author believes that confidentiality and discretion are indispensable attributes of any kind of negotiations, thus full publicity and transparency in this regard are hardly conceivable.

The relevant critique for the purposes of this thesis revolves around the fact that most of the fora for investment arbitration envisage in camera proceedings, do not require cases to be registered, do not allow the participation of non-parties in the proceedings, and preclude the publication of the awards, by the tribunal or the arbitral framework, without parties’ consent. Such approach, developed for private commercial arbitration, is aimed at the speedy, ‘business-like’ resolution of disputes. However, due to the aforementioned vertical nature, i.e. dispute taking place not between two juridical equals, but between private party and a State, in relation to the latter’s assumption and assertion of sovereign authority, this model does not fit the system well and seems to undermine its overall legitimacy.

Yet since early 2000’s there is a discernible move towards greater transparency in arbitral proceedings borne, inter alia, out of the cultural phenomenon of the information age. Although it would be naïve to believe that arbitration in a fishbowl will ever be reached, drawing on the improvement proposals it might be possible to diminish some of the fears attached to the lack of transparency of ISDS that have been floating around. The exact nature and scope of these proposals are discussed below in a selective fashion.

3. 2. 1. Possible ways to overcome the lack of transparency

As mentioned before, the talks about the establishment of greater transparency and openness in investment arbitration have gained traction for well over a decade. In 2001, the three NAFTA signatories issued a Note of Interpretation in which they made transparency the default

130 Ibid.
133 This term to describe the full transparency of investment arbitration was coined by Calvin William Sharpe, see, Sharpe, Arbitration in a Fishbowl: The Ethics of Disclosure, Speech at the Annual Meeting of the National Academy of Arbitrators, 2005, available at http://naarb.org/proceedings/pdfs/2005-228.PDF (1st June 2014).
provision in all investor-state complaints brought under NAFTA Chapter 11. ICSID, for its part, revised its Arbitration Rules in 2006, including norms aimed at increasing transparency, as did the PCA in 2012 by adopting Arbitration Rules, which accommodated visible concessions to transparency. Many new BITs, inter alia, those of the US and Canada, also tend to include pro-transparency clauses. And very recently UNCITRAL unveiled a brand new set of Rules on Transparency in treaty-based investor-State Arbitration (Rules on Transparency), which came into effect from 1st of April 2014. Moreover, the Working Group II of the UNCITRAL has begun preparatory works for the Convention on Transparency, which would allow signatories to express their consent to the application of new Rules on Transparency to all investment treaties already in force. Underlying this evolution is the hope that increased public awareness will allay suspicions that arbitral secrecy allows ‘backroom dealings’ in matters of public concern, and will contribute to the legitimacy of investment arbitration by enhancing public confidence in the fairness and integrity of the arbitral process.

The concrete proposals of how to increase the transparency in arbitral proceedings abound. They range from the ones, which are directed towards greater public participation in the proceedings, to those, which are intended to make corps of arbitration more transparent. Yet due to a limited scope of this thesis only three essential proposals, including public access to arbitral documents, public access to arbitration proceedings and the possibility for third parties to submit amicus curiae briefs will be examined more closely in this chapter. Later the examination of whether the EU is receptive towards the general transparency trends in investment arbitration and is using it as a tool to answer to the mounting public criticism of the system will be conducted.

3. 2. 1. 1. Public access to arbitral documents

The rules, procedure and practice of documents’ disclosure in investment arbitration largely reflect those found in commercial arbitration. This means that in investor-State arbitration such disclosure still remains subject to parties’ consent for the most part. Thus, the knowledge that views and arguments made by the parties and adjudicators can be read and picked apart by anyone, which is indispensable to the accountability and independence of judges, especially where they are deciding questions of sovereign authority and the allocation of taxpayer funds, is missing in the system.

However, the general rule of non-disclosure is changing. Approaching this issue in a comparative fashion reveals that in NAFTA arbitration regime after the FTC gave its

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134 Bianchi/Peters, Transparency in International Law, p. 153.
135 The 2004 US Model BIT contains a separate clause on Transparency of Arbitral Proceedings, as does the Canada Model Foreign Investment Promotion and Protection Agreement (FIPA).
140 Van Harten (fn. 60), p. 161.
interpretation on 31st of July, 2001\textsuperscript{141}, the public has nearly unfettered access to the relevant documents generated during the course of NAFTA Chapter 11 arbitrations, apart from confidential and otherwise protected information\textsuperscript{142}. Such trend is said to be driven by the US and Canada’s strong legal cultures and structures guaranteeing access to government information\textsuperscript{143}. ISCID Convention, for its part, provides that the ICSID should not publish the award without the consent of the parties\textsuperscript{144}. In practice, though, even when such consent is not given by one of the parties, most of the arbitral awards are published elsewhere, and ICSID publishes excerpts of legal holdings. There are no express rules concerning disclosure of other documents in ICSID Convention, and the case-law, generated by non-disputing parties, wishing to gain access to such documents in order to produce \textit{amicus} submissions afterwards, points towards the tendency not to disclose pleadings and written memorials for the general public\textsuperscript{145}.

The new UNCITRAL Rules on Transparency, which have now become an integral part of UNCITRAL Arbitration Rules\textsuperscript{146}, but can also work as a stand-alone instrument for other arbitral rules, lay down a progressive set of pro-transparency clauses. Article 2 of UNCITRAL Rules on Transparency foresees that as soon as the arbitral proceedings commence, basic procedural information – names of the parties, economic sector involved and the underlying treaty – has to be disclosed to the public by the repository. Article 3 of these Rules further provides a catalogue of disclosable documents, dividing them into mandatory automatic disclosure (all statements and submissions by the disputing parties and non-disputing State parties or third persons; transcripts of hearings; and orders, decisions and awards of the arbitral tribunal), mandatory disclosure on request of any person (witness statements and expert reports) and the disclosure of documents which rests on the discretion of a particular tribunal (exhibits) categories. Article 7, for its part, is an exception and provides that some information, \textit{inter alia}, confidential business information and the one, which could impede law enforcement, is exempted from being disclosed. The final authority to decide if certain type of information falls under the exception clause is given to the tribunal and is to be decided on a case-by-case basis.

As can be inferred from above, the new UNCITRAL Rules on Transparency give access to a wealth of documents and is arguably able to provide more accountability and public involvement in the ISDS. On the other hand, it also carries the danger of re-politicizing dispute settlement fora and make it lose its allure for prospective disputants. Furthermore, it is also probable that increased transparency will change the way parties to the proceedings draft their pleadings and the number and extent of the documents they will be eager to disclose to the public’s eye.

\textsuperscript{141} The NAFTA parties have generally agreed that nothing in the NAFTA imposes the general duty of confidentiality on the disputing parties to a Chapter 11 arbitration, see, NAFTA Free Trade Commission, Notes on Interpretation of Certain Chapter 11 Provisions, § 1, 31 July, 2001, available at \url{http://www.state.gov/documents/organization/38790.pdf} (21st May 2014).

\textsuperscript{142} \textit{Menaker} (fn. 138), p. 134.

\textsuperscript{143} \textit{Brower}, Berkeley J. Int'l L. 2010 (Vol. 5), p. 23.

\textsuperscript{144} Article 48 (5) of ICSID Convention (2006 revised version).

\textsuperscript{145} \textit{Suez, Sociedad General de Aguas de Barcelona, S.A. and Vivendi Universal, S.A. v Argentine Republic}, ICSID Case No. ARB/03/19 and \textit{Biwater Gauff (Tanzania) Ltd. v United Republic of Tanzania}, ICSID Case No. ARB/05/22.

\textsuperscript{146} The \textit{ratione temporis} of UNCITRAL Rules on Transparency according to their Article 1 (1) is directed to the future unless the Parties agree otherwise. This means that they do not automatically apply to the large swath of already existing investment treaties, although the above described UNCITRAL Convention on Transparency is being drafted in order to change that temporal limitation.
3. 2. 1. 2. Public access to arbitration proceedings

Another related issue to the perceived lack of transparency in the ISDS, is the public’s ability to observe arbitral hearings. As a general rule, arbitral hearings take place in camera, however, the practice has shown that it is possible to conduct such hearings in an open and transparent manner enabling the general public to have a greater degree of scrutiny.

The NAFTA text is silent on whether non-disputing parties may observe arbitral hearings, which has led the FTC to yet again express its general endorsement of open hearings in NAFTA Chapter 11 Arbitrations\(^{147}\). However, the opening of arbitral hearings still remains subject to the claimant’s consent and is not granted all the time. As of today, several hearings under the auspices of NAFTA have been open to the public, with the Methanex case\(^{148}\) being the prime example. All of these cases were administered by ICSID, and their hearings were broadcast to publicly accessible rooms in the World Bank\(^{149}\).

The ICSID Arbitration Rules have historically disfavored open hearings absent mutual party consent, and, not surprisingly, parties have rarely jointly consented to open ICSID hearings\(^{150}\). The revised version of Arbitration Rules 2006, though, amended respective Rule 32 (2) and set the default rule to be the one of open hearings. Put differently, whereas the old Rule 32 allowed tribunals to open hearings to non-party attendance only if the two parties consented, the new Rule 32 gives tribunals the authority to open hearings to attendance or observation as long as no party raises objections\(^{151}\). Thus, explicit consent of parties is not a necessity anymore, but the disputing parties still retain their veto powers.

The Article 25 (4) of an old version of UNCITRAL Arbitration Rules provide that hearings shall be held in camera unless the parties agree otherwise. However, with the new Rules on Transparency a revolutionary step has been taken. Not only does Article 6 of these Rules provide that hearings, save for the part where confidentiality of information or integrity of the proceedings need to be protected, or for logistical reasons, shall be open, but it also does not foresee a right for disputing parties to veto open hearings. Such legal novelty clearly shifted the presumption from confidentiality to openness and will boost democratic participation to a great extent.

3. 2. 1. 3. Third-party written submissions

Finally, the ability of non-disputing parties to submit amicus curiae briefs to arbitral proceedings bears discussion. The concept of amicus curiae is accepted in a number of domestic legal systems and has more recently became recognized in various international proceedings\(^{152}\).

\(^{147}\) Initially only the US and Canada supported this endeavour, yet in NAFTA FTC’s Joint Statement - “A Decade of Achievement” released on 16 July, 2004, it was finally recognized that all signatories of this treaty support open hearings for investor-state disputes, available at http://www.ustr.gov/archive/Document_Library/Press_Releases/2004/July/NAFTA_Free_Trade_Commission_Joint_Statement - A Decade of Achievement.html (22nd May 2014).

\(^{148}\) See Methanex Corporation v. United States of America, UNCITRAL (1976), Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005.

\(^{149}\) Menaker (fn. 138), p. 136.

\(^{150}\) Sauvant, Yearbook on International Investment Law & Policy 2009-2010, p. 257.

\(^{151}\) Ibid.

Even though this concept *per definitionem* is not restricted to a particular form, in the given context it is to be understood as the submission of written briefs.

The ability of third-parties to intervene and to file submissions was yet again firstly given serious consideration under NAFTA Chapter 11 regime. Since NAFTA text is silent on this matter, it had to be resolved in the case-law. In already mentioned *Methanex* case, taking place under UNCITRAL auspices, the tribunal found that it had authority to accept *amicus* briefs under the so-called residual procedural power granted by Article 15 (1) of UNCITRAL Arbitration Rules, which *inter alia* provides that the arbitral tribunal may conduct the arbitration in such manner as it considers appropriate. The same authority was reaffirmed in a subsequent *UPS* case arbitration, also governed by UNCITRAL Arbitration Rules. Such arbitral practice evolved into ‘legislative response’ with NAFTA FTC issuing an interpretation of 7 October 2003 in which the NAFTA States effectively approved the participation of *amici curiae* in NAFTA arbitration proceedings. Alongside with this interpretation, the concrete non-binding procedural recommendations how *amicus* submissions should be drafted were passed. Additionally, previously mentioned 2004 US Model BIT and 2004 Canada’s Model FIPA recognized the usefulness of *amicus* submissions and incorporated express clauses regarding them.

The revised version of 2006 ICSID Arbitration Rules, for its part, changed Rule 37 (2) and established Tribunal’s authority to allow to file a written submission with the Tribunal regarding a matter within the scope of the dispute, even without a consent of disputing parties. This clause is not a *carte blanche* for any kind of submissions to be accepted, though. It enshrines substantive criteria, which are designed to help the Tribunal to decide whether to allow such a filing, and procedural safeguards, ensuring that disputing parties are treated equally and written submissions do not unduly burden the proceedings.

The new UNCITRAL Rules on Transparency now expressly affirm the right of a third-party to file a written submission with the arbitral tribunal regarding a matter within the scope of the dispute (Article 4 (1)), while providing concrete guidelines for parties wishing to make such submission (Article 4 (2) and Article 4 (4)). Article 4 (3) also lays down factors to be taken into consideration by the Tribunal in determining whether to allow third-party submissions, such as the significant interest of a third-party in the proceedings and the extent to which such submission can assist the Tribunal. Finally, Article 4 (5) and Article (6) foresee procedural safeguards, which are placed to guard the integrity of the proceedings and the principle of equality of arms. In the author’s view, all the criteria and procedural safeguards provided serve the purpose of ensuring that the inclusion of third-party submissions in the proceedings is not discretionary, thus it does not arbitrarily disfavor any disputing party, well.

Not only does the permission of *amici* intervention increase legitimacy of investment arbitration, but such third-party submissions can also contribute to the substantive legal quality of arbitral awards. For example, in some cases disputing parties may have specific vested interests not to disclose all the facts and details relevant to the issues in dispute. Such situation

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155 Article 28 (3) of 2004 Model US BIT and Article 35 (1) Canada’s Model FIPA.

156 Levine (fn. 152), p. 217.
can then be rectified by successful intervention of non-parties. Besides, amici can bring their exclusive expertise to the proceedings and introduce public interest considerations such as human rights, environmental protection and public health. This contribution has already been endorsed by the arbitral jurisprudence, stating that submissions from amici were “useful and informative”\textsuperscript{157}. Moreover, there is a discernible trend that nowadays third-party interveners do not confine themselves to be NGOs only, but are much more diversified. In one case even the EC has successfully sought to enjoy the right of being an amicus in order to represent EC’s interest in enforcing competition law\textsuperscript{158}. Such diversified\textsuperscript{159} legal input of various actors is always welcomed.

However, as many other legal novelties, the acceptance of third-party submissions is also charged with negative consequences. The permission of non-disputing parties to file submission can create very practical burdens, such as rising costs and expediency of the proceedings. In extreme cases it can even have the capacity to breach the principle of equality of arms. Thus, infusing arbitration with third-party submissions should not unduly burden the whole proceedings and clearly-defined criteria of written briefs worthy to be included therein need to be crystalized.

\subsection{3.2.2. The EU’s position on the transparency challenge}

The EC in its public consultation document on ISDS-into-TTIP\textsuperscript{160} recognizes transparency as essential for the legitimacy and accountability of the system and identifies the lack of it as a main challenge to the current ISDS. Transparency, as a component of the state-of-art ISDS is also envisaged in the Directives for the negotiation on TTIP\textsuperscript{161}. The EC goes further to emphasize that it took the leading role in establishing new UNCITRAL Rules on Transparency, incorporated them into CETA and is willing to do so in TTIP as well. Such position coincides with a recent EU’s decision to fund new international transparency database, which should increase transparency and accessibility of investment disputes to the public even more\textsuperscript{162}.

In the reference text on transparency issue (question No. 6) in the public consultation document the EC juxtaposes the non-existence of transparency provisions in modern BITs with a text developed in CETA (Article x-33: Transparency of Proceedings). Not only is it clear from this juxtaposition that the EU intends to incorporate new UNCITRAL Rules on Transparency into TTIP to the disclosure of information to the public concerning disputes (Article x-33 (1)), but it is also willing to expand some of the provisions foreseen therein. Namely – Article x-33 (2) injects additional documents (the request for consultation, the request for a determination, the

\textsuperscript{157} See, Biwater case (fn. 145), para 392.
\textsuperscript{158} See, AES Summit Generation Limited and AES-Tisza Erd\'ma Kft. v. Republic of Hungary (AES), ICSID Case No. ARB/07/22, Decision on Award, 23 September 2010, para 8.2.
\textsuperscript{159} Article 4 (3) (b) of the new UNCITRAL Rules on Transparency expressis verbis provides that in determining whether to allow an amicus submission Tribunal pays attention if perspective, particular knowledge or insight of amicus is different from that of the disputing parties. The same rule is also to be found in leaked CETA text, Article 3 (2) (b) of Annex I.
\textsuperscript{160} European Commission, Public consultation on modalities for investment protection and ISDS in TTIP (fn. 12).
\textsuperscript{161} Council of the European Union (fn. 13), para 23.
notice of determination, the agreement to mediate, the notice of intent to challenge, the decision on an arbitration challenge, the request for consolidation) into the disclosable documents’ catalogue foreseen in Article 3 (1) of the UNCITRAL Rules on Transparency. Moreover, Article x-33 (3) goes one step further and lists ‘exhibits’ as documents to be made available to the public, which is excluded by the Article 3 (2) of the UNCITRAL Rules on Transparency.

It is also noteworthy, that Article x-33 of CETA introduces different moment, counting from which the disclosable documents should be promptly made available for the public. While Article 2 of UNCITRAL Rules on Transparency provides that the disclosure should follow ‘once a notice of arbitration has been received by the respondent’, Article x-33 (4) enshrines that relevant information should be disclosed ‘prior to the constitution of the tribunal’.

Apart from these two modifications, the proposed Article x-33 (5) of CETA also encompasses the general rule to open hearings to the public, however, is silent on the possibility for amici to submit briefs. The latter provision, though, is to be found in the leaked version of CETA, namely – in the Article 3 of Annex I, which grants the arbitral tribunal the authority to allow the filing of submissions for the third-parties and sets guidelines on the form and content of such amicus briefs, amongst other things.

Overall it must be concluded that transparency in ISDS is treated as a serious objective by both contracting parties of the TTIP. The US, as a flagship of NAFTA, experienced and later adopted pro-transparency innovations into its model BITs first-hand, whereas the EU with its newly gained competence over FDI became a vocal advocate of transparency by significantly contributing to the launch of UNCITRAL Rules on Transparency. Considering such legislative path dependence, as well as concrete pro-transparency achievements already implanted in the CETA, it is safe to conclude that such inclination towards transparency in the ISDS system will continue from both sides of the Atlantic. The presumption from confidentiality to transparency in the ISDS system has been changed and is unlikely to be undone. Thus, the myth of ‘secretive off-shore tribunals’ in the ISDS-into-TTIP rhetoric should be debunked. However, it must be borne in mind that transparency will not be a panacea for all ills. Indeed, it might prevent progress on certain fronts because the ability of disputing parties to settle disputes might be adversely affected by premature publicity, for example, when the parties harden their position due to the influence of extrinsic powers. Yet again a balance between public’s interest to be involved in matters of public concern and investors’ interests of settling disputes in a neutral forum must be struck.

3.3. The independence and impartiality of arbitrators ruling in ISDS cases

“Regardless of whether they are ‘distinguished former judges’, ‘respected scholars and practitioners’, or ‘former government officials’, all arbitrators lack the independence of the most junior tenured judge”

Gus Van Harten

Another big part of criticism concerning ISDS system is directed to the corps of arbitration, i.e. actors entrusted with the right to settle disputes. The critics point out that the

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system is missing basic components of judicial independence, such as the security of tenure or flat salary of the arbitrators\textsuperscript{164}, even though arbitrators’ sovereign decision-making role is in key respects more determinative than that of a domestic judge\textsuperscript{165}. The lack of these core elements of judicial independence renders arbitrators to be susceptible to undue influences and external pressure.

Moreover, the investment-treaty arbitrators are usually selected on a case-by-case basis by political or economic entities. Arbitrators depend on senior officials at the organizations that are designated as appointing authorities under investment treaties, the prime examples being the ICSID, the ICC International Court of Arbitration and the Arbitration Institute of Stockholm Chamber of Commerce\textsuperscript{166}. In other words, the selection of arbitrators who later rule on the legality of sovereign acts is conducted by executive officials or business representatives. Thus, they have perceived pro-business bias. Such bias is further exacerbated by the fact that arbitrators’ chances of re-appointment depend on the investors’ willingness to sue States hosting their investment in the future. Put differently, the more investment arbitrators rule in favour of the claimants or interpret loosely worded investment protection standards in a broad (claimant-friendly) fashion, the bigger the incentives and chances of investors bringing more claims to adjudicate. However, there are some critics of this argument pointing out that arbitrators want to establish reputation for being unprejudiced in arbitration world\textsuperscript{167}, thus they are disinclined to adopt manifestly biased decisions and engage in a practice called ‘baby-splitting’, i.e. awarding partial victories to both disputants.

Finally, arbitrators frequently combine their role with several other hats: working as practitioners, academics, policy advisers or as media commentators\textsuperscript{168}. Such engagement in remunerative activities outside adjudication means that the same arbitrators can be counseling the company as attorneys one day and sitting on arbitral bench ruling on the merits of the claim the same company initiated against sovereign States – another day. This double-hat syndrome yet again obviously undermines judicial independence and its sister concept – judicial impartiality\textsuperscript{169}, even though, in words of one Indian lawyer “standards of behavior expected of arbitrators are no less stringent than those demanded of judges; in fact arbitrators are expected to behave a shade better since judges are institutionally insulated by the established court-system, their judgments being also subjected to the corrective scrutiny of an appeal”\textsuperscript{170}.

\textbf{3.3.1. The options for reforming the arbitration corps}

Yet as with other systemic problems of an ISDS set out above, improvements can and ought to be made. The proposals for reform of the arbitration corps vary from those that

\textsuperscript{164} The guiding catalogue of components of judicial independence can be found in UN Basic Principles on the Independence of the Judiciary adopted by the Seventh UN Congress on the Prevention of Crime and the Treatment of Offenders held at Milan from 26 August to 6 September 1985 and endorsed by General Assembly resolutions 40/32 of 29 November 1985 and 40/146 of 13 December 1985.
\textsuperscript{165} Van Harten (fn. 131), p. 633.
\textsuperscript{166} Van Harten (fn. 60), p. 164.
\textsuperscript{168} Burley (ed.) (fn. 109), p. 36.
\textsuperscript{169} Independence can be understood as freedom from control, whereas impartiality means freedom from bias.
\textsuperscript{170} Nariman, Arbitration International 1988 (Vol. 4, No. 4), pp. 311 – 312.
encourage to inject basic institutional safeguards into the system to those, which purport that a clear set of rules for possible misconduct and necessary qualifications of arbitrators is necessary or those, which seek to find an objective method of appointing arbitrators in order to free them from unwarranted influences.

The author of this thesis is skeptical about the prospects of including conventional institutional safeguards in the ISDS and immunizing arbitrators from external pressures in such a way because investment treaty arbitration was always bric-á-brac and never had one institutional home. It is hard to conceive how tenure or flat salary could be introduced also in the ISDS-into-TTIP context since the prospective caseload pertinent to this treaty would be rather limited for a great number of arbitrators to be tenured on a long-term basis. Moreover, it would be naïve to believe that high-profile arbitrators would subscribe themselves to the system which would potentially prohibit lucrative outside activities or cap the remuneration for them. However, it is possible to find an objective method of appointing arbitrators and there are other proposals how to improve the corps of arbitration. The most important of these proposals are discussed below. In no way does such listing of viable options for reform pretend to be exhaustive or fix all ills, however, in the author’s view, if implemented, it could significantly discipline the most important actors of the system, foster the confidence and integrity of an ISDS and help to counter the critique of it being ‘the world’s worst judicial system’ significantly.

3.3.1.1. Adoption of the code of conduct for arbitrators

The main proposal of how to improve arbitration corps is the one which encourages the adoption of a code of conduct for arbitrators. The ultimate goal of such code of conduct in investment arbitration would be to improve the fairness of the process and to secure the integrity of – and public respect for – the outcome.

In the province of commercial arbitration the first AAA/ABA Code of Ethics for Arbitrators in Commercial Disputes was originally promulgated already in 1977 and reworked in 2004. In a similar vein, the IBA has also adopted its Rules of Ethics for International Arbitrators in 1987 and IBA Guidelines on Conflicts of Interest in International Arbitration in 2004, alongside with many regional initiatives to establish codes of such kind. All these instruments, despite being non-binding in nature, have found wide acceptance in arbitration society. However, ignoring such developments in commercial arbitration, investment arbitration, for its part, still “dwells in an ethical no-man’s land”, even though some investment treaties do contain professional qualifications, one of which is independent judgment.

There are many discussions about the exact content of possible ethical code for investment-treaty arbitrators, yet for the purposes of this thesis, suffice it to say that the general duty to behave in an independent and impartial way and the duty to disclose interests should be included. The first provision, albeit encompassing two standards of behavior which are difficult

171 This term was coined by a non-profit organization called Third World Network (TWN).
172 Available at https://www.adr.org/aaa/ShowProperty?nodeId=/UCM/ADRSTG_003867 (1st June 2014).
175 Milan Chamber of National and International Arbitration and Singapore International Arbitration Centre can be mentioned among institutions that have promulgated ethical codes for arbitrators.
177 García-Bolívar (fn. 113), p. 4.
to define, would impose a modicum of self-discipline on arbitrators. To solidify this general obligation of a moral character, arbitrators before appointment or confirmation could sign a statement indicating their independence and file it with the authority in charge. In case arbitrators fail to fulfill this duty – this statement could be used to make them liable.

The second provision would ensure that all parties are aware of contacts and relationships arbitrator enjoys that may hinder his or her impartiality to make a decision. In other words, such disclosure is a guarantee of ensuring that justice will be done – and be seen to be done – on an independent and impartial basis. The duty to disclose interests, embedded in such code of conduct, would also help to solve the double-hat syndrome and expose arbitrators who are riddled with conflicts. As a consequence, arbitrators from law firms whose major income comes from representing multinational enterprises in making and carrying out foreign investments should desist from arbitrating.

It is not possible to lay down an exhaustive list of all interests and contacts of an arbitrator that might cloud his or her independence or impartiality, thus alongside the general rule to disclose past and present professional, business and other relationships (if any) with the parties, the drafting of an overall rule of disclosing circumstances which may likely give rise to reasonable doubts as to the independence or impartiality of an arbitrator could be complemented. The criterion of ‘a reasonable person’, i.e. that of an objective observer, for evaluating what can be considered to raise reasonable doubts about arbitrator’s independence or impartiality as a yardstick can be included.

Additionally, in order for provisions to be effective, a clear challenge procedure and a mechanism for disqualification of arbitrators for their manifest lack of independence and impartiality should be included.

178 The similar mechanism is envisaged in Article 11 (2) of ICC Rules of Arbitration, providing that before appointment or confirmation, a prospective arbitrator shall sign a statement of acceptance, availability, impartiality and independence.


180 Such dual role of arbitrators as impediment to their impartiality was successfully challenged in recent case-law, where an arbitrator was also acting as managing partner and a member of steering committee of a global law firm representing claimant’s interests in concurrent proceedings, see, Blue Bank International & Trust (Barbados) Ltd. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB 12/20, 12 November 2013, Decision on the Parties’ Proposals to Disqualify a Majority of the Tribunal.


AAA/ABA Code of Ethics for Arbitrators in Commercial Disputes prescribes that all arbitrators should disclose any known existing or past financial, business, professional or personal relationships which might reasonably affect impartiality or lack of independence in the eyes of any of the parties (Canon II (A)), whereas arbitral case-law uses ‘reasonable person’ instead of ‘the eyes of the parties’ standard, see, Suez et al. v. Argentina, para. 46.

184 Such ‘manifest lack’ criteria is enshrined in Article 57 of the ICSID Convention, however, some critics point out that this test is in need of greater conceptual clarity, see, Crawford, Challenges to Arbitrators in ICSID Arbitrations, Confronting Global Challenges: From Gunboat Diplomacy to Investor-State Arbitration, PCA Peace Palace Centenary Seminar, 11 October 2013, available at http://www.pca-cpa.org/showfile.asp?fil_id=2398 (4th June 2014).
3. 3. 1. 2. Qualification requirements for arbitrators

Another practical solution how to improve arbitral corps is to set adequate qualification requirements for those adjudicating disputes between investors and sovereign States. Traditionally, the ability to choose arbitrator is the manifestation of a party autonomy. Even more so, it is often claimed that the quality of arbitration proceedings depends to a large extent on the quality and skill of the arbitrators chosen\textsuperscript{185}. The parties are free to nominate and appoint an arbitrator from a particular background or with a particular expertise deemed to be the best suitable for resolving dispute at issue. As an outcome of this freedom to choose, investment treaty panels have been criticized for being “manned by commercial arbitrators whose concern for the values of the international community is weaker than their concern for contractual sanctity <…> and their loyalty to the values of multinational business”\textsuperscript{186}.

This perception is confirmed by the Article 14 (1) of ICSID, which states that arbitrators shall be persons of high moral character and recognized competence in the fields of law, commerce, industry or finance, who may be relied upon to exercise independent judgment. It can be seen that whereas economic fields besides law in the article are highlighted, no particular requirement of knowledge of areas that are pertinent to the investment disputes is attached.

Due to the reasons already mentioned – the asymmetric nature of the system and the subject matter of the disputes – it is crucial to contemplate the inclusion of new qualification requirements to the pool of investment-treaty arbitrators, such as environmental or human rights law. Thus, the expansion of epistemic communities, described in the previous chapter, could be practically attainable.

3. 3. 2. EU’s approach to arbitrator ethics, conduct and qualifications

The EU in its public consultation on modalities for investment protection document acknowledges the double-hat syndrome, which may lead to a conflict of interests and is also apprehensive of the critique voiced that the arbitrators may not have the qualifications necessary to rule on matters of public interest or on matters that require a balancing between investment protection and, for example, environment, health or consumer protection.

In order to tackle these problems the EU is resolved to introduce specific requirements in the TTIP on the ethical conduct of arbitrators, including a binding code of conduct, which will also accommodate the removal of arbitrator for his or her failure to abide by the rules set therein. Moreover, if the arbitral award is already rendered and a breach of the code of conduct is found, it can lead to a possible reversal of that ISDS founding. The EU is also willing to set up a roster, i.e. a list of qualified individuals from which the chairperson for the ISDS tribunal is drawn, if the investor or the responding state cannot otherwise agree to a chairperson. Accordingly, the responding state chooses one arbitrator and has vetted the third arbitrator.

From the text provided as reference (Article x-25 and Article x-42 of CETA), couple of inferences can be drawn. Firstly, it can be seen that ISDS tribunal typically will comprise of three arbitrators, however, the possibility of a sole arbitrator settling the dispute is not ruled out (Article x-25 (1)). In this case, the agreement of disputing parties on the sole arbitrator is requisite. In the case of three-strong panel, the designation should happen as follows: one

\textsuperscript{185} Lew/Mistelis/Kröll, Comparative International Commercial Arbitration, p. 232.

arbitrator shall be appointed by each of the disputing parties and the third, who will be the presiding arbitrator, shall be appointed by agreement of the disputing parties. If the efforts to constitute an arbitral panel within 90 days fail, the authority to appoint the arbitrators may be transferred to the Secretary General of ICSID (Article x-25 (2)). He or she shall appoint the arbitrators from a special roster set up by Article x-25 (3). In the event that such list has not been established on the date a claim is submitted to arbitration, the Secretary-General of ICSID shall make the appointment at his or her own discretion taking into consideration nominations made by either Party and, to the extent practicable, in consultation with the disputing parties.

In the author’s view, the latter provision could be modified by transferring the ultimate authority for appointing arbitrators to a more neutral institutional body. ICSID, being a part of World Bank and having its Secretariat funded by it, is oftentimes criticized for acting as a proxy for affluent investors. Thus, delegating such authority to, for example, ICJ which is a judicial arm of universal international organization, would eliminate pro-corporate bias in the public’s eye and lend the system additional layer of legitimacy.

Article x-25 (3) also makes clear that the general presumption is not to allow an individual, who is a national of either EU or Canada, to be presiding arbitrator of the panel unless parties agree otherwise. However, Article x-25, read systematically, leaves a right for the disputing parties to appoint arbitrator of the same nationality as non-presiding member of the panel. This possibility is a welcome achievement, echoing the idea that the presence of a national arbitrator on the bench can bring social and political context of a country hosting claimant’s investment to the dispute and foster the subsequent acceptance of arbitral award in its society.

Another positive achievement of CETA is the roster of at least 15 suitable arbitrators, which is pursuant to Article x-25 (3), read in conjunction with Article x-42, to be established and maintained preferably no later than the entry into force of the CETA, and in any event no later than two years after the entry into force of the CETA. Such roster of arbitrators, albeit not being an institutional safeguard, can serve two-fold aim: firstly, it can provide suitable arbitrators with more stability that can insulate them from undue incentives to favour one of the parties and increase their independence as a result; secondly, it can bolster up transparency since the eligible arbitrators will be publically known.

It is noteworthy, that only individuals who comply with requirements set forth in Article x-25 (5) can be included in a roster. It states that such individuals shall have expertise or experience in public international law, in particular international investment law and it is desirable that they have expertise or experience in international trade law, and the resolution of disputes arising under international investment or international trade agreements. While highlighting knowledge of public international law, as a qualification requirement of suitable arbitrators, is commendable, more qualification requirements relating to knowledge of societal and public policy issues could be attached in the future. In this way, the expansion of epistemic communities, contemplated above could come to fruition and the particular concerns pertinent to the regulatory matters of the State could be better taken count of. However, bearing current reality of arbitration world in mind, i.e. the fact that most of arbitrators come from private law background, it is also understandable that the drafters of CETA did not want to shrink the pool of eligible and competent arbitrators drastically and formulated this requirement in a broad manner.

To ensure the independence of arbitrators, Article x-25 (6), besides inter alia enshrining the general duty to be independent and not affiliated with or take instructions from any disputing party for arbitrators, provides that arbitrators shall comply with the IBA Guidelines on Conflicts

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of Interest in International Arbitration or the proposed code of conduct, which is to be adopted. Such inclusion of already existing ethical rules and a prospective code of conduct for arbitrators, which is fortified by a challenge mechanism foreseen in Article x-25 (7), (8), (9) and (10), in the author’s view, reflects state-of-the-art approach to transparency challenges in the ISDS. Between the two options – a specific code of conduct should be given priority and its adoption should be accelerated because it is capable of addressing matters specific to investment-treaty arbitration, whereas IBA Guidelines on Conflicts of Interest in International Arbitration was established in the realm of commercial arbitration.
Conclusion

The main purpose of this thesis was to investigate ISDS, which with the advent of TTIP negotiations seems to have become an anathema of various NGOs, and see whether the critique it receives is reasonable from a legal point of view.

After exploring the history and genesis of an ISDS, alongside with its general rationale and the problems stemming therefrom, as well as ISDS position in the EU’s investment architecture, three perceived deficiencies, which have been circulating in the general ISDS-into-TTIP discourse the most – ISDS’s interference with a State’s right to regulate, lack of transparency and arbitrator ethics, conduct and qualifications – formed the core of analysis. Not only were these perceived drawbacks discussed and measured in detail, but the constructive proposals how to overcome them in a practical way were offered and an investigative glimpse into the CETA text, as a best analogy to the TTIP available, was casted.

From the research conducted using historic, textual, systemic and comparative methods, couple of key findings bear to be highlighted. Firstly, it can be inferred that an ISDS has been borne out of investors’ quest for a neutral dispute resolution forum in lieu of diplomatic protection, which failed to be an effective remedy in a system where financial stakes were high. The ISDS’s coming-of-age was fueled by a ‘treatification’ process, which resulted in the patchwork of various BITs and EU’s after-Lisbon push forward generated by its wish to make use of a newly gained competence and set a ‘golden standard’ for upcoming negotiations with economic powerhouses, such as India and China.

The genesis of an ISDS also revealed that despite the public law character in investment-treaty arbitration, it is piggybacking on the procedure established by commercial arbitration, which undermines the legitimacy of the system. What is more, there was little debate around nascent ISDS and the general public was eventually presented with a fait accompli, which seemed to cause frustration and a sense of exclusion and prevented from the possibility to carry out substantial ISDS reform. In this regard, the EC’s decision to freeze ISDS-into-TTIP talks for 3 months is a positive development capable of allowing public to finally have its say.

Despite the lack of debate in the past, the current criticism ISDS encounters is fierce. One of the most heavily criticized aspect of an ISDS is its interference with an inherent State’s right to regulate public matters through so-called ‘chilling effect’. The analysis conducted in thesis has shown that this point of critique is hugely overblown and that the ‘chilling effect’ is a political and not a legal one. Moreover, it is unlikely to take place due to the formal absence of precedent in the investment arbitration, lack of authority of arbitral tribunals to nullify contravening national laws and incoherence of the whole structure. The analysis also revealed that this popular fear can be tamed by making vague investment protection standards more determinate and by including express clauses reaffirming State’s right to regulate public matters, which has already become a commonplace. Such general escape clause is also foreseen to be included into TTIP and drawing on CETA experience, it is plausible that it will protect a wide array of policy areas from the undue encroachment of investors’ interests. Yet more public law instruments can be used in extinguishing this popular concern of investment provisions being able to kill regulations, such as the inclusion of deferential standards – proportionality, good faith requirement or margin of appreciation – into escape clauses. Furthermore, the expansion of epistemic communities by bringing forward more arbitrators coming from public law background and arbitrators sharing the same nationality with the responding State could take place.
Another big part of criticism – the lack of transparency in the ISDS – turned out to be exaggerated by the general public as well. The research has demonstrated that there is a constant discernible move towards greater transparency in arbitral proceedings since early 2000’s and that the presumption of confidentiality has been switched to the one of openness. Most of the pro-transparency innovations, including public access to arbitral documents, public access to arbitration proceedings and third-party submissions – were contemplated by the US, as a flagship of NAFTA. What is more, the EU has also taken a leading role in the pro-transparency movement by advocating the adoption of the new UNCITRAL Rules on Transparency and even funding new international transparency database for ISDS. Drawing on this legislative path dependence and on CETA example, which has shown that the EU made these UNCITRAL Rules on Transparency to be an integral part of the system, it is very likely that the pro-transparency attitude will be upheld in the TTIP as well. Thus, the myth of secretive off-shore tribunals in the ISDS-into-TTIP rhetoric has to be debunked for most of the arbitral documents and arbitral proceedings will be open to public, and the amicus curiae submissions – allowed.

Finally, the corps of arbitration, including arbitrator ethics, conduct and qualifications, and the proposals for reform were examined. The examination has led to a conclusion that while pro-corporate bias and double-hat syndrome of arbitrators remain significant challenges attributable to the actors of the ISDS system, the improvements thereof are viable. Amongst them – the adoption of a code of conduct for arbitrators and the inclusion of new qualification requirements – seem to be the most crucial ones. Investigating EU’s receptivity to them in the CETA text, has shown that it is willing to render corps of arbitration more accountable by making them to abide to AAA/ABA Code of Ethics for Arbitrators in Commercial Disputes or to its very own code of conduct, which is ought to be adopted no later than 2 years after CETA’s entry into force. What is more, a roster of 15 arbitrators will be established, which not only will partly insulate arbitrators from unwarranted extrinsic pressures, but also bolster up transparency. However, while these are all welcome developments, the analysis of CETA text has also revealed the need to tie more stringent qualification requirements to the arbitration corps, such as knowledge of societal and public policy issues in order to respond to the nature of investment-treaty arbitration better. Finally, the ultimate authority to appoint arbitrators, in case of disagreement between parties, should be transferred to a more neutral body, for example – the ICJ, rather than ICSID, as foreseen by CETA, in order to eradicate pro-corporate basis.

Even though, currently the inclusion of an ISDS into TTIP has been suspended and the future of it remains unclear, an educated guess that it is possible to reconcile it with a popular fear of corporations ‘suing the living daylights out of governments’ can be made. As demonstrated by this thesis, to every point of critique uttered by the general public, solutions of improvement can be found starting with public law instruments, which are capable of augmenting legitimacy of the system. Thus, not a complete overthrown of an ISDS but rather a constructive dialogue between two opposing camps should be fostered.
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