INTERNATIONAL POLICY ANALYSIS

Investment Protection at a Crossroads

The TTIP and the Future of International Investment Law

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- For years, intergovernmental investment agreements have been concluded which grant foreign investors extensive rights to sue states before private international tribunals. In recent times, the number of actions taken by investors has risen sharply. The »infringements« by states that are punishable in investor-state disputes have expanded so that actions are being increasingly directed against laws that were drafted democratically, in the public interest and in accordance with national law.

- Existing investment protection rules jeopardise public finances through the threat of actions for damages. They bypass the rule of law with their private parallel law for corporations and represent an encroachment on the regulatory autonomy of states. They undermine democracy in favour of the private property rights of foreign investors.

- With the debate surrounding the transatlantic trade agreement TTIP, the controversy over global investment law has well and truly arrived in Europe. The European Commission has temporarily suspended the negotiations on investment protection and has launched a public consultation on the issue. However, this consultation does not deal with the issue of whether investor protection is even needed in an EU-US agreement, but only with how it should be structured.

- Nevertheless, the current politicisation of the issue in the EU also presents opportunities for a fresh start in investment policy without unilateral investor rights to sue states in private tribunals and without special property rights for foreign investors that go beyond constitutional guarantees of the protection of property, but with binding obligations on investors, such as duties to respect human rights and workers' rights.

Dialogue on Globalization

Contents

With the debate surrounding the transatlantic trade agreement (Transatlantic Trade and Investment Partnership, TTIP), the controversy over global investment law has well and truly arrived in Europe. Criticism of this »parallel justice in the name of money« (Pinzler et al. 2014)[1] is growing especially in Germany – extending even into the mainstream media and the conservative party camps. However, resistance to TTIP is also being ignited outside of Germany primarily by the planned special rights of litigation for corporations.

Worldwide there are already numerous international treaties containing these investor-state dispute settlement rights. They enable foreign investors to bring lawsuits against countries before private international arbitral tribunals – on account of any policy that threatens their property titles and the planned profits from their investments, whether because of health and environmental regulations or as a result of social and economic policies that restrict their entrepreneurial freedom.

Thus, the Swedish power company Vattenfall is currently suing Germany because it is not happy with the nuclear phase-out. In Australia and Uruguay, Philip Morris is taking legal action against tobacco control policies. And the Canadian oil and gas company Lone Pine is suing its own government through a US subsidiary because the province of Quebec has declared a moratorium on the deep drilling technique known as fracking on account of environmental risks associated with natural gas exploration.[2]

The lawsuits are not heard before ordinary state courts, but before ad hoc private international tribunals. The three private individuals of whom the tribunals are usually composed are appointed by the parties to the dispute, and they operate in accordance with the arbitration rules specified in the relevant investment agreements. They have the power to review all measures taken within a state – laws enacted by parliaments, executive decisions and court verdicts – as regards their compatibility with the extensive investors rights, and to order states to pay large sums in damages. Their rulings are binding and can be enforced worldwide. There are no provisions for appeals procedures.

No ordinary court in the world has as much power. The arbitral tribunals violate important constitutional principles: the independence of the arbitrators is not guaranteed; their meetings are generally closed to the public, being held in hotel rooms in London, Paris or New York; and their rulings are for the most part secret. Moreover, the relative positions of the parties to the disputes are extremely unequal: investors only have rights and feature as plaintiffs, states only have obligations and hence are always the defendants. Investor protection treaties do not contain provisions for investor duties (for example, to respect human rights, workers' rights or environmental standards).

In the case of the transatlantic trade agreement, investor-state arbitration poses incalculable risks. Already today, over half of the foreign direct investment in the United States and the EU comes from the other side of the Atlantic. There are umpteen thousand subsidiaries of US corporations in Europe and vice versa. According to research by the organization Public Citizen (2013), investor-state dispute settlement rights enshrined in an EU-US agreement would enable 75,000 companies, either directly or through foreign subsidiaries, to attack more progressive legislation on health, environmental and workplace safety on the other side of the Atlantic. It is no wonder that the head of the domestic affairs department of the German newspaper *Süddeutsche Zeitung,* Heribert Prantl, recently described the planned exclusive special rights for large-scale investors as a »*clandestine coup d'état«,* as one of »the most dangerous assaults ever launched on democracy and the welfare state« (Prantl 2014). It is no wonder that the opposition to the TTIP is united in rejecting this »transatlantic corporate bill of rights« (Corporate Europe Observatory/Transnational Institute/Seattle to Brussels Network 2013).

In an attempt to take the wind out of its critics' sails, the European Commission has suspended negotiations on investment protection in the TTIP for the present. A public consultation on the issue was launched at the end of March 2014 which ran until the beginning of July (European Commission 2014). However, this consultation does not deal with the issue of *whether* and *why* investment protection is even needed in an EU-US agreement, but only with *how* it should be structured. Thus, the Commission's concern is not with a free and open-ended discussion, but only with polishing and selling its agenda. The consultation nevertheless opens up a space for a more

1. All translations of quotations from German sources are by the translator.

2. See Box 1 (p. 6) for examples of ongoing lawsuits and Box 2 (p. 11) for examples of already concluded lawsuits.

thorough-going debate on rules of global investment protection. Its outcome will have implications not only for the agreement between the EU and the US, but also for the global struggle against the »globalization of corporate power« (Mies/von Werlhof 2003): If social movements, trade unions, environmental organizations and other critics of investment arbitration manage to keep the latter out of the TTIP, that will provide a boost to social movements and left-wing governments throughout the world which are trying to limit the power of transnational corporations and to break out of neoliberal adhesion contracts concluded in the past. On the contrary, if the EU successfully anchors its »reformed« investor rights in the TTIP, this will enhance the legitimacy of the globally contested investment protection regime. In an attempt to situate the debate, I will begin by reviewing the development of international investment law. In a second step, I will present problem areas of the legal field and offer some political-economic classifications. In the third section, I will outline current fractures in and conflicts over the regime of international investment law. Finally, I will trace an arc back to the current controversy within the EU: With whom is the EU negotiating on the issue of investment protection at present? What should we make of the reform agenda of the Commission? And what options are there for action leading to a more democratic, socially just and environmentally sustainable investment policy?

1. The Historical Development of International Investment Law

Neither transnational corporations nor global production chains would exist without foreign investment. It offers direct access to sales markets, technologies, and cheap raw materials and labour. Since it has a decisive influence on the relations of production and social relations in the recipient countries once it reaches a certain scale, it is a major factor in global power relations.

Since the postwar period, there has been an increase in intergovernmental agreements that impose certain obligations on the treaty parties in dealing with investments and investors from the other country. Such agreements can stipulate, for example, that states must immediately pay compensation for expropriations or for »measures tantamount to expropriation«, and that they grant investors direct rights to sue them before an international tribunal in cases of conflict. More than 3,200 such agreements exist worldwide, most of them on a bilateral basis (Bilateral Investment Treaties, BITs). According to the UN organisation for trade and development (United Nations Conference on Trade and Development, UNCTAD), in recent years one new investment agreement has been concluded on average per week (UNCTAD 2013: 4).

Initially, these consisted almost exclusively of North-South agreements. In the 1950s and 1960s, capital exporting countries wanted to protect their investors in their former colonies through such agreements. In the 1970s, the agreements were part of the defence against aspirations to changed economic relations, as expressed in the Declaration on the Establishment of a New International Economic Order. Finally, in the 1990s, there was a real race to invest in parts of the global South that led to an explosive increase in investment agreements. This race was fostered by the dependence on private capital flows as a consequence of the debt crisis of the 1980s, the increasingly neoliberal orientation of the programs of the International Monetary Fund (IMF) and the World Bank, as well as of the dominance of neoliberalism during this period. Accordingly, the central provisions in investment agreements are based on the idea of the »game of wealth creation« (Friedrich August von Hayek) of private capital flows in a free market immunised against state interventionism and the vagaries of democratic politics, but in need of strong, government-backed property rights in order to develop.

Why do states sign treaties that set such severe restrictions on their sovereignty? Why do they invest private tribunals with the power to review their actions, to award damages and to severely restrict government regulations? The answer involves a mixture of interests, misconceptions and ignorance – interests, because it is in the interest of capital-exporting countries to protect »their« companies abroad; misconceptions because above all developing countries hoped for more foreign investment from the treaties. However, it remains a matter of dispute whether the agreements actually lead to more investment. Quantitative studies yield contradictory results. And qualitative studies suggest that the treaties play no, or only a marginal role in the investment decisions of companies. When the EU Commission (2010: 28) polled 300 European companies, half of them did not even know what an investment agreement is.[3]

3. For a review of the literature, see Poulsen (2010).

The promise of investment often remained unfulfilled in practice as well. When South Africa recently began to cancel bilateral investment treaties (BITs), an official declared: »We do not receive significant inflows of FDI from many partners with whom we have BITs, and at the same time, we continue to receive investment from jurisdictions with which we have no BITs. In short, BITs are not decisive in attracting investment« (Raman, 2012).

In addition to the panacea of more investment, lack of awareness of the political and economic risks of investment treaties is also an important explanation for why government enter into such agreements. In the past, negotiations often lasted only a couple of hours. Sometimes lawyers, let alone officials from ministries of justice, were not even involved. The admission by a former Chilean negotiator can serve as an example: »like most countries in the 1990s, we signed a lot of treaties not knowing sometimes what we were committing ourselves to« (Poulsen 2013: 10). The risks often become apparent only many years later when the country becomes the target of a lawsuit.

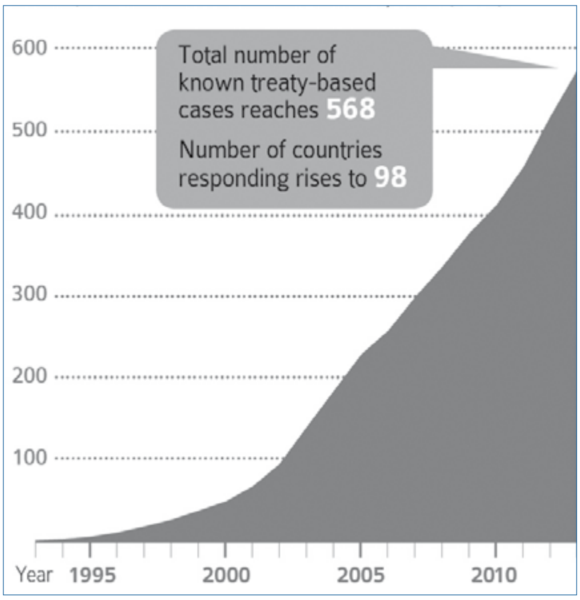
Even today, the global South most frequently finds itself in the dock in investor-state disputes. According to UNCTAD (2014: 7–8), around three-quarters of all of lawsuits that became known by the end of 2013 were directed against developing and emerging countries; in the overwhelming majority of cases – 85 per cent – the plaintiff was an investor from the global North. Argentina and Venezuela are the countries that have been most often hauled before investment arbitration tribunals. However, in times of changed capital flows, industrialised countries increasingly often also have to defend themselves: Czech Republic is now the third most frequently sued country, with Canada ranking sixth; and almost half of the new investor-state actions initiated in 2013 are directed against industrialised countries, most of them EU member states (ibid.: 1). This trend is likely to continue, also due to the growing number of north-north investment and free trade agreements with investment protection chapters, such as the proposed agreement between the EU and the United States.

The »infringements« by states that are punishable in investor-state actions were gradually extended over the past two decades. While originally arbitrary expropriations and discrimination against foreign investors provided grounds for actions, the latter are increasingly directed against laws that were drafted democratically, in the public interest and in accordance with national law.

That these actions have any prospect of success is a result of the vaguely-formulated, but far-reaching guarantees of protection of property for investors in international investment law (Krajewski 2013, Hoffmann 2013). For example, some tribunals interpret the standard of »fair and equitable treatment« in such a way that authorities from the local to the national level always have to act completely transparently and consistently and must not disappoint the »legitimate expectations« of investors regarding the regulatory environment of their investments (Bernasconi-Osterwalder/Liu 2013). Moreover, whereas protection against »indirect expropriation« in this form is not a feature of most national constitutions, this right, anchored in investment agreements, guarantees foreign investors compensation if their property loses value as a result of regulations. Thus, a fracking moratorium is as open to attack as the German nuclear phase-out (see Box 1).

Several factors have significantly increased the risk of states being sued in recent years. First, investor-state lawsuits have become better known in the corporate world, with the result that there has been a corresponding explosion in the number of lawsuits – from a dozen in the mid-1990s to 568 known lawsuits at end of 2013

Deluge of Disputes: Cumulative Number of Cases



Quelle: UNCTAD, Down to Earth

Box 1: Examples of Current Investor-State Actions

Corporations against health protection – Philip Morris v. Uruguay and Australia: Since 2010, Philip Morris has been suing Uruguay, and since 2011 Australia. Both of these suits are directed against plain packaging for cigarettes and health warnings designed to reduce tobacco consumption. The case against Australia is being conducted via a Hong Kong subsidiary – based on the investment protection agreement between Hong Kong and Australia. Uruguay is being sued by Philip Morris International with headquarters in Switzerland – based on the Switzerland-Uruguay Agreement. The tobacco company wants 2 billion US dollars in compensation from Uruguay, around 4 per cent of the gross domestic product of the country. The amount of the damages beings sought from Australia is not known. In both cases, Philip Morris is also calling for a suspension of tobacco control laws. (Martin 2013)

Corporations against the nuclear phase-out – Vattenfall v. Germany (II): Since 2012, the Swedish power company Vattenfall has been suing the German government on the basis of investment protection rules in the multilateral Energy Charter Treaty. Vattenfall wants over 3.7 billion euros in compensation for the decommissioning of the Krümmel and Brunsbuttel nuclear power plants in the context of the German nuclear phase-out following the Fukushima disaster. Both of these fault-prone reactors were already off line when the German parliament passed the law to phase out nuclear power. This is already the second action that Vattenfall has brought against Germany (see Box 2). (Bernasconi-Osterwalder/Hoffmann 2012)

Corporations against environmental protection – Lone Pine v. Canada: The oil and gas company Lone Pine has been suing Canada since 2012 for 250 million Canadian dollars in damages. Because of the danger of environmental destruction posed by fracking, the province of Quebec issued a moratorium on the controversial deep drilling technique and in this context revoked a number of drilling licenses. Lone Pine is headquartered in Canada, but it is suing the country through a letterbox company in the US tax haven of Delaware based on the investment protection provisions in the North American Free Trade Agreement (NAFTA) between the US, Canada and Mexico. (Attac et al. 2014: 5)

Corporations against water protection – Pacific Rim v. El Salvador: Since 2009, the mining company Pacific Rim has been conducting a lawsuit against a mining moratorium in El Salvador based on the investment protection rules in the Central America Free Trade Agreement (CAFTA) between the United States and several Central American countries. The moratorium was imposed following massive popular protests against environmental destruction and water pollution from mining activities. Because Pacific Rim cannot open its planned gold mine »El Dorado« as a result, the corporation wants 301 million US dollars in compensation for the loss of the expected profits, hence about 1 per cent of the gross domestic product of the country. Pacific Rim is headquartered in Canada (which is not a party to CAFTA) and is conducting its action through a subsidiary in the US state of Nevada.[4]

Corporations against compensation for environmental crimes – Chevron v. Ecuador: Since 2009, the US multinational oil company Chevron has been suing Ecuador on the basis of the United States-Ecuador investment agreement, because it had been sentenced by Ecuadorian courts to pay 9.5 billion US dollars in compensation to indigenous communities for massive environmental pollution – wrongly, according to Chevron. To date, the three-man tribunal which is hearing the case has found in favour of the corporation and has called upon the government of Ecuador not to carry out the sentence. The fact that Ecuador has rejected this by appeal to the separation of powers in its constitution is now being interpreted by Chevron as a violation of the standard of »fair and equitable negotiation« in investment law – for which Chevron is in turn seeking compensation.[5]

Corporations against the debt haircut – Poštová Banka & Istrokapital v. Greece: The Slovak Poštová Banka and its Cypriot shareholder Istrokapital have been suing Greece since 2013 on account of the haircut on the country's sovereign debt. In 2010, Poštová Banka had bought Greek government bonds at a knockdown price. When Greece was negotiating a reduction of the debts with its creditors two years later, the bank opposed the haircut. The legal basis for the action is provided by bilateral investment agreements between Greece and Slovakia and between Greece and Cyprus. The level of damages demanded is not known. (Corporate Europe Observatory/Transnational Institute 2014: Chapter 3).

Corporations against the minimum wage – Veolia v. Egypt: Since 2012, the French utility company Veolia has been suing Egypt based on the bilateral investment agreement between France and Egypt for an alleged breach of a contract for waste disposal in the city of Alexandria. The city had refused to make changes to the contract which Veolia wanted in order to meet higher costs – in part due to the introduction of a minimum wage. In addition, according to Veolia, the local police had failed to prevent the massive theft of dustbins by the local population. According to media reports, Veolia wants 82 million euros in compensation. (Karadelis 2012)

Corporations against the Arab Spring – Indorama v. Egypt: Since 2011, the Indonesian textile group Indorama has been suing Egypt because an Egyptian court ordered the re-nationalization of a textile factory that had been privatized – according to the court, unlawfully – under the Mubarak regime. The judgement had been preceded by a strike and occupations by textile workers calling for the re-nationalization of the company and for better working conditions and wages. (Perry 2011)

Corporations against patent law – Eli Lilly v. Canada: The US pharmaceutical company Eli Lilly has been conducting an action since 2013 against Canada's patent law on the basis of the investor protection in NAFTA, because Canadian courts had declared two of its patents on medicines void. The patents for Strattera to treat attention deficit and hyperactivity disorder and Zyprexa to treat schizophrenia were revoked because the promised benefit had not been adequately demonstrated in a short test phase with a small number of test persons. Eli Lilly wants 500 million US dollars in compensation and is also attacking Canadian patent law, according to which a patent is granted only if the promised benefits of an invention can be adequately proven at the time of the patent application. (Trew, 2013)

Corporations against environmental protection – Renco v. Peru: Because the mining company Doe Run had not satisfied the promised environmental protection measures at a metal smelting plant in the town of La Oroya in the Peruvian Andes, the government revoked its operating licence. As a result, the corporation has been conducting a lawsuit since 2011 based on the bilateral United States-Peru free trade agreement through its US parent, the Renco Group, for 800 million US dollars in damages. Environmental organizations have repeatedly declared La Oroya to be one of the most polluted places in the world. The levels of lead, cadmium and arsenic in the blood of children living there are far too high. (Public Citizen 2012)

4. For up-to-date information on the lawsuit, see: http://www.miningwatch.ca/categories/company-country-issue/company/pacific-rim.

5. See the campaign of the Ecuadorian Government »The Dirty Hand of Chevron«: http://apoya-al-ecuador.com/en/history-of-texaco-in-ecuador/.

(UNCTAD 2014: 1). The actual figure is likely to be considerably higher due to the lack of transparency of the system. And the number is set to increase. In 2013 alone, 57 new actions were initiated, according to UNCTAD (ibid.), only one less than in the previous year, a record year for newly initiated actions.

This wave of lawsuits has made investment arbitration into a lucrative business for the legal profession (Corporate Europe Observatory/Transnational Institute 2012), which also increases the risk of litigation. With hourly rates of up to 1,000 US dollars for lawyers in investor-state proceedings, it is not surprising that law firms continually encourage their multinational clientele to bring suits – for example, when states take measures to combat economic crises. The commercial arbitrators, who earn more the more cases that are brought, tend to interpret vague investment law broadly, and hence in favour of the investor, which increases the chances of future lawsuits (see 2.3). Finally, law firms and hedge funds reduce the financial risk for plaintiffs, because they conduct »litigation funding« as a business and assume the legal costs in investor-state lawsuits, only to collect portions of the compensation paid to the investor later.

A third development that has led to an increase in the risk of litigation in recent years is the trend towards »investment structuring« or so-called »treaty shopping« by means of an extensive network of foreign subsidiaries, in part created for this purpose. Thus, an investor A can make an investment in country B through a subsidiary in country C, for example, if an especially investor-friendly agreement exists between countries B and C – and then sue country B on the basis of this agreement. The result of this investment structuring are lawsuits such as that of the Canadian corporation Lone Pine, which is suing its home country Canada through a letterbox company in the United States (see Box 1).

2. Problem Areas of International Investment Law

In the following, four problem areas of investment law and investment arbitration will be distinguished: a) the risks for public finances and the taxpayer, b) the risks for the regulatory autonomy of the state, c) constitutional problems in the context of the privatization of law, and d) the threats to democracy.

2.1 The Threat to Public Finances

The dangers posed by investor-state lawsuits for public finances and for taxpayers are manifest: they can lead to compensation payments running into billions of dollars or euros. The costs incurred by states in this connection are continually increasing: in 2012, an arbitral tribunal ordered Ecuador to pay historically unprecedented damages to the tune of 2.4 billion US dollars (including interest and legal costs). That is just under 3 percent of the country's gross domestic product and corresponds to the annual national health spending for seven million Ecuadorians (Public Citizen 2012a). The US company Occidental had brought – and won – a lawsuit because the country had unilaterally revoked its oil extraction contracts with the company.

The legal fees for investor-state lawsuits alone can drain the public purse. According to the OECD (2012: 19), they amount to 8 million US dollars on average per case, though they can also be considerably higher. According to media reports, the Philippine government has spent 58 million US dollars on its defence against two lawsuits brought by the airport operator Fraport – money with which they could have paid 12,500 schoolteachers or simply built two new airports (Olivet 2011: 4). Since to date the arbitral tribunals have tended to have the parties foot their own legal bills, a country may have to shoulder the legal costs even when it does not lose a lawsuit. The European Commission wants to change this, however, and to stipulate that the losing party has to bear all of the legal costs. As it happens, the German government has made a provision of 6.5 million euros to cover litigation fees and retainers for its defence against the ongoing Vattenfall suit. According to a question time in the German parliament, almost 700,000 euros have already been spent; 2.2 million euros have been earmarked in the 2014 budget, 2 million for 2015 and 1.6 million for 2016 (Deutscher Bundestag 2014: 32).

2.2 Encroachments on the Regulatory Autonomy of the State

A second problem area is the pressure exerted by investment agreements and investor-state lawsuits on state regulations. Sometimes even the threat of a lawsuit is enough to stifle or dilute pending legislation – »regulatory chill« as this is known in the jargon. Five years after the NAFTA free trade agreement between Mexico, Canada and the United States came into force, a Canadian government official described the phenomenon as follows: »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 and proposition in the last five years. They involved dry-cleaning chemicals, pharmaceuticals, pesticides, patent law. Virtually all of the new initiatives were targeted and most of them never saw the light of day« (quoted in Greider 2001).

In fact, companies seem to be using international investment law today more as a weapon or for »pre-emptive strikes« in political disputes surrounding regulation than as a protective shield against encroachments by the state.[6] Thus on two occasions in Canada tobacco control laws were shelved after the tobacco industry had threatened to bring NAFTA lawsuits. In Indonesia, companies were exempted from a ban on mining in the rainforest after they had threatened to bring a corresponding case against the state before an arbitral tribunal.[7] Vattenfall also achieved the dilution of an environmental restriction imposed on the controversial coal-fired power station in the Hamburg district of Moorburg (see Box 2) in the context of the settlement in its first investment lawsuit against Germany. And the New Zealand government has announced that it will delay the implementation of its tobacco control laws pending a decision in the action taken by Philip Morris against Australia (see Box 1).[8] Even if the tobacco company loses this lawsuit, it will nevertheless have achieved the desired effect, namely delaying legislation to reduce tobacco consumption in other parts of the world at least for a couple of years. Philip Morris's profits will continue to flow freely during this time – with society as a whole incurring increased costs for health care spending.

Aside from diluting, preventing and delaying regulations, investor-state litigation can lead to the profits that individual companies have lost as a result of policy reforms being socialised, even when the regulations in question are necessary to protect the public interest. According to American author William Greider (2001), that is precisely the function of the investor rights in agreements such as NAFTA: they are part of a »long-term strategy, carefully thought out by business« to redefine »public regulation as a government ›taking‹ of private property that requires compensation«. In other words, those who regulate should pay.

Central for this »new international super basic right to unhindered exercise of investment« (Prantl 2014) is the usual protection in investment agreements against »indirect« expropriation and »regulatory takings«, thus protection against measures which, it is argued, have a similar economic effect to the seizure of property. The consequences of this doctrine of protection against indirect expropriation are far-reaching, according to Greider – and intentional: »Because any new regulation is bound to have some economic impact on private assets, this doctrine is a formula to shrink the reach of modern government and cripple the regulatory state – undermining long-established protections for social welfare and economic justice, environmental values and individual rights. Right-wing advocates frankly state that objective – restoring the primacy of property against society's broader claims« (Greider 2001).

The range of policy measures that are open to attack based on a doctrines such as the protection against indirect expropriation has been vividly described by two lawyers from the law firm Luther – as it happens, in a brochure published by the former German government with the alarming title *Help, I'm been expropriated!* In this brochure, one can read: »The potential diversity of harmful state action is virtually unlimited« and taken as a whole can indeed be tantamount to expropriation. For example, the state could introduce new taxes that make it economically pointless to continue to conduct a specific business; or it could enact environmental laws that prohibit previously manufactured goods or reduce state-regulated tariffs, for instance in the electricity, gas or telecommunications sectors or in toll roads, and thus destroy the financing of a project (Germany Trade and Invest 2011: 5).

2.3 Circumventing the Rule of Law

Investment arbitration involves a privatized legal system modelled on the arbitral procedure for resolving disputes between two companies. This »shadow justice in luxury hotels« (Henrich et al., 2013) is completely unsuitable for

6. Zachary Douglas, then still at Cambridge University and now a solicitor at the firm Matrix Chambers, mentioned this trend at the conference »50 Years of Bilateral Investment Treaties« in Frankfurt, 1.–3.12.2009.

7. For this and further cases, see Tienhaara (2011).

8. Turia, Turiana: »Government moves forward with plain packaging of tobacco products«, February 19, 2013; http://www.beehive.govt.nz/release/government-moves-forward-plain-packaging-tobacco-products.

reviewing all state regulatory instruments and rulings concerning damages reaching into the millions or billions, for which the taxpayer ultimately has to foot the bill.

To recall, no regular court in the world has as much power as the private tribunals that decide on investor-state lawsuits. One of the arbitrators described this vividly: »When I wake up at night and think about arbitration, it never ceases to amaze me that sovereign states have agreed to investment arbitration at all (…) Three private individuals are entrusted with the power to review, without any restriction or appeal procedure, all actions of the government, all decisions of the courts, and all laws and regulations emanating from parliament« (quoted by Corporate Europe Observatory/Transnational Institute 2012: 34).

The »constitutional perversion« (Prantl 2014) represented by private arbitration is made apparent by the break with central constitutional principles: of equality before the law,[9] transparency of procedures[10] and procedural fairness[11] Moreover, it involves a one-sided parallel law in which only investors can take actions, but not the state, when investors, for example, violate human rights or pollute the environment. No obligations are imposed on investors.

In this asymmetrical legal system, the breach of the principle of judicial independence becomes especially problematic. The cases are not heard by regular courts with judges who enjoy tenure and cannot be removed from office in the case of »unwelcome« judgments. Before such a regular court, it would be decided in advance or through a randomised procedure which judges would receive which cases. Their salaries would be assured regardless of their judgements and the number of cases they heard. These are all important institutional safeguards for judicial independence.

Investor-state cases, by contrast, are heard by ad hoc tribunals which are generally made up of three private persons appointed by the parties to the dispute and paid an hourly or daily fee per case. In the most widely-used institution for legal actions taken by investors, the Washington International Centre for Settlement of Investment Disputes (ICSID), the arbitrators earn 3,000 US dollars per day (ICSID 2013: 1). For the most part, the same arbitrators are appointed over and over again. They are known by insiders as the »club« or the »inner mafia« (quoted from Corporate Europe Observatory/Transnational Institute 2012: 36, 38). A mere 15 of them decided 55 per cent of the investor lawsuits that became known by the end of 2011 (ibid.: 38).

This points to a tangible conflict of interests. More investor-state claims ensure that these »entrepreneurial arbitrators« (Menon 2012: 15) receive more nominations and remuneration in the future. In an asymmetrical legal system in which only one side (the investor) can take actions, this is a major incentive to keep the system litigation-friendly through rulings and legal interpretations favourable to investors. An empirical study of 140 investment protection lawsuits showed that the arbitrators do in fact tend to interpret certain clauses expansively, and hence in favour of the investor (van Harten 2012). An example of an investor-friendly interpretation of the concept »foreign investor« is, for example, recognising a 98 per cent Ukrainian-owned company as a Lithuanian investor and allowing an investor-state lawsuit against Ukraine based on its investment protection agreement with Lithuania.[12]

The lack of independence and the propensity to make investor-friendly legal interpretations shows that the alleged neutrality of private arbitration, which is continually invoked by its proponents, leaves a lot to be desired. Arbitral tribunals are simply not »fairer«, to quote a recent headline from the *Frankfurter Allgemeine Zeitung* – as it happens, penned by a former investment protection lawyer (Bubrowski 2014). The inherent bias of arbitration also makes clear that there will not be »easy reforms leading to a better system« (Griebel 2014), as long as the interpretation of the law is entrusted to a private judicial machinery with a financial and career interest (see point 4).

2.4 Erosion of Democracy

The ultimate aim of investment law is to place restrictions on counter-hegemonic forces and democracy. A quote from two lawyers from Milbank (Nolan/Baldwin

9. The private courts are only for »foreign« investors; »normal« businesses and people have to make do with »normal« courts.

10. Like the arbitral awards, they are generally secret.

11. Affected third parties, such as a municipality against whose decision an action is being brought, have no right to information, to express their views or to have them taken into consideration.

12. This is what happened in Tokios Tokelés v. Ukraine (ICSID Case No. ARB/02/18).

2012: 49), one of the leading law firms in international investment law, makes this clear: »Adverse government actions do not have to take place only with autocratic rule. The populism that democracy can bring often is the catalyst for such actions.« It is no wonder that countries like Argentina and Ecuador that have revoked privatisations and nationalised companies following fierce social unrest, are among the countries that have most often been the targets of lawsuits in investment arbitration.

The research program on »new constitutionalism« which is deeply influenced by Stephen Gill is suitable for a critical analysis of international investment law. It studies political-juridical structures that safeguard neoliberalism and existing property relations through quasi-constitutional restrictions on the scope for state intervention and democratic control. The political is being redefined as a result – for example, when investment policies are depoliticised and removed from democratic control by enshrining economic principles in investment agreements.

Democracy is also being curtailed by absolutising private property rights and privileging foreign investors. Only foreign investors – or those who »heave« themselves into such a status by structuring their investments accordingly (see above) – have the opportunity to intervene in political debates over regulations by threatening to bring expensive investor-state lawsuits in a parallel legal system to which they alone have access and in which states are regularly ordered to make high compensation payments. Compared with other social groups – unions, domestic companies, citizen initiatives – this gives them a great deal of power to influence political decisions in their own interest. Only they can appeal to the excessive protection of private property in investment law, which is broader than that enshrined in most national constitutions, and is blind to the social responsibility of ownership (see, among others, Hoffmann 2013). Thus whereas »compensable de facto expropriation« does not exist in the German constitution (Dederer 2012), according to investment law indirect appropriation always calls for compensation – even if it promotes a public purpose. Anticipated future profits are not deemed to be part of private property worthy of protection under German law either, whereas investors are regularly awarded compensation for the expected profits they have lost in investor-state lawsuits.

Another effect of investment agreements is the constitutional codification of what Joachim Hirsch has called the »internationalised competition state«, whose function is less that of a controlling instance of economic actors than to gear the national and regional levels to global competition by harmonising policies. The legal scholar David Schneiderman (2008) has studied this taking the example of numerous constitutional changes (in Latin America, for example) through which, as a result of an investment agreement, conceptions of property that restrict private property rights for the purpose of social redistribution by the state were displaced from national constitutions in favour of the liberal conception. As a result, the state is being strengthened in its function as an enforcement mechanism of private property rights, while its redistributive and social policy competences are being truncated.

3. Fractures in the International Investment Law Regime

However, these procedures are not free of contradictions. On the contrary, there are unmistakable fractures in and fierce conflicts over the international investment law regime. Social movements successfully scandalise individual cases;[13] critical researchers denounce the risks for government regulation, public finances and democracy (e. g. Public Statement on the International Investment Regime 2010); and some states have turned their backs on parts of the regime and are trying to create alternatives. Even among proponents of the regime there is talk of a crisis of legitimacy that needs to be addressed (e. g. Waibel et al. 2010).

Above all in the global South, resistance is growing to the neoliberal supra-constitution of international investment law. South Africa has cancelled agreements with several EU countries, including Germany, and declared that further treaties from the post-apartheid era, which the country had hastily concluded at the time in the hope of attracting investment, will follow. Indonesia has recently initiated similar steps. According to media reports, India is drafting a model agreement for investment protection that is supposed to differ markedly from the models of the post-colonial era and of the 1990s and 2000s.

13. For an overview, see the website of the Network for Justice in Global Investment: http://justinvestment.org.

Box 2: Examples of Concluded Investor-State Lawsuits

Companies against anti-discrimination – Foresti et al. v. Republic of South Africa: In 2007, Italian and Luxembourg investors sued South Africa for 350 million US dollars in compensation, because a new mining law contained antidiscrimination elements in favour of blacks from the Black Empowerment Act. According to this law, the investors would have had to sell shares in the company to »historically disadvantaged South Africans«. The case was declared to be closed in 2010 after the investors had received new licenses, requiring a much lower divestment of shares. (IAPP 2011)

Corporations against nature conservation – Metalclad v. Mexico: The US waste disposal company Metalclad sued Mexico in 1997 on the basis of the NAFTA agreement for 90 million US dollars in damages. The background was the expansion of a waste disposal plant for toxic waste in a Mexican municipality. Although the facility had been approved by the Mexican government, the municipality had subsequently ordered a suspension of building work and the federal state declared the area to be a nature conservation zone. Metalclad sued on the grounds of expropriation and won 16.2 million US dollars in compensation. (Public Citizen 2014: 22)

Corporations against policies to combat economic crises – Investors v. Argentina: Argentina was sued a total of 41 times on account of measures it took to combat its economic crisis in 2001/2, including the devaluation of the peso, caps on water, gas and electricity charges, as well as debt restructuring measures. Up to January 2014, the country had been ordered to pay a total of 980 million US dollars in compensation. The legal defence costs in a case that is still pending alone amount to 12.4 million US dollars. (Corporate Europe Observatory/Transnational Institute 2014: 12).

Corporations against environmental and health protection – Ethyl vs. Canada: When the Canadian Parliament banned the import and transportation of a toxic petrol additive on environmental and health protection grounds in 1997, the US producer Ethyl sued on the basis of the NAFTA agreement for 201 million US dollars in compensation. Canada agreed in a settlement to pay 13 million US dollars and withdrew the trade restrictions. (Public Citizen 2014: 11)

Corporations against environmental protection – Vattenfall v. Germany (I): In the case brought in 2009 over 1.4 billion euros compensation based on the Energy Charter Treaty, the bone of contention was the coal-fired power station in the Hamburg district of Moorburg which was controversial on climate policy grounds. Vattenfall considered the requirements imposed for removing cooling water from the Elbe river to be too strict. The case was settled in 2011 by mutual agreement after the environmental requirements for Moorburg had been relaxed. The legal dispute over the power station in the German domestic courts continues. (Bernasconi-Osterwalder/Hoffmann 2012)

Corporations against national courts – Deutsche Bank v. Sri Lanka: In October 2012, an arbitral tribunal ordered Sri Lanka to pay 60 million US dollars in compensation plus interest and 8 million US dollars legal costs to Deutsche Bank for breaches of the investment agreement between Germany and Sri Lanka. Because of allegations of corruption, the highest court in the country had decreed that payments to the bank, which would have been due according to a hedging agreement with the state oil company, should be suspended. The decision has whetted appetites in the financial sector because it recognises a financial market instrument as an investment worthy of protection – even though it did not involve any physical business activity by Deutsche Bank in Sri Lanka. (King & Spalding 2013)

Bolivia, Ecuador and Venezuela have cancelled a number of investment agreements and withdrawn from the ICSID convention which establishes the centre of the same name at the World Bank. In Ecuador, a commission is examining whether the country's agreements are compatible with national law. At a meeting of the countries of the Bolivarian Alliance for the Peoples of Our America (ALBA) in April 2013, a review of existing treaties was likewise agreed, as well as the establishment of a separate regional institution for resolving conflicts with foreign investors.

A paradigm shift is also taking place in some industrialised countries and international organizations. The social-democratic Gillard government in Australia had declared in 2011 that it would no longer negotiate investor-state arbitration in its free-trade agreements. The conservative successor government has also recently signed an agreement with Japan which does not include investor-state dispute settlement. And whereas the UNCTAD urged countries of the South to sign investment agreements especially during the 1990s, in recent publications (2012, 2013a) it outlines options for reforming current investment policies – ranging from more clearly circumscribed rights for investors to duties for investors. In addition to UNCTAD (2013b: 3-4), even the IMF (2012: 42) now warns that investment agreements can severely restrict states in combating economic and financial crises.

4. The Debate within the EU over the Future of Investment Law

The debate over investment policy at European level has now broken out in the midst of this tough struggle over global investment law. Until the Treaty of Lisbon entered into force in December 2009, the EU did not have any authority to negotiate investment protection treaties and corresponding chapters in free trade agreements. This was the sole responsibility of the EU member states, which to this day are world champions in this area: they have concluded around 1,400 of the over 3,200 investment agreements worldwide; no country has more bilateral treaties than Germany (139, of which 131 are in force).[14] Moreover, investors based in the EU are assiduous litigants: most of the investor-state lawsuits that attracted worldwide attention were indeed brought by investors from the United States (127 lawsuits), but they are followed by investors from the Netherlands (61 lawsuits), the United Kingdom (43 lawsuits) and Germany (39 lawsuits) (UNCTAD 2014: 8).

A controversy has been raging since 2009 over how investment protection should be designed in future across the EU. The provisional result of the debate is a series of corporation-friendly guidelines and mandates for investment protection negotiations between the EU and Canada, India, the United States, Japan, Morocco, Tunisia, Egypt, Jordan, China and the ASEAN countries (Brunei, Myanmar, Cambodia, Indonesia, Laos, Malaysia, the Philippines, Thailand, Singapore and Vietnam).

A number of non-governmental organizations were able to use the negotiations with the United States to politicise the issue and mobilise large sections of civil society against the transatlantic corporate bill of rights. The European Commission (2013) is responding to this politicisation with an aggressive PR campaign which is designed to allay the public's concerns and promises a »new start« on the issue of investment protection. Vaguely-worded investor rights, such as »fair and equitable treatment« or protection against »indirect expropriation«, are supposed to be clearly defined, the state's »right to regulate« to be protected and the dispute settlement procedures to become transparent and independent. Lawsuits such as those of Philip Morris against tobacco control laws in Australia and Uruguay would no longer be possible under the reformed investor rights, according to the Commission.

Closer examination of the reform proposals reveals that this is not the case.[15] First, the supposedly watertight definitions of investor rights continue to contain many loopholes for broad, investor-friendly interpretations by arbitrators. Thus, for example, the general clause »fair and equitable treatment« is framed even more broadly than for instance under the NAFTA agreement. This is extremely dangerous, because this catch-all clause has developed into an all-purpose weapon for investors with which they win most lawsuits (Bernasconi-Osterwalder/Liu 2013). The Commission now wants to extend the standard so that it expressly protects the »legitimate expectations« of an investor. Could tax increases disappoint the »legitimate« expectations of an investor when previously low tax rates promised fat profits? Could a moratorium on fracking contradict the fair and equitable treatment of a gas company if a government had previously signalled its support for the controversial drilling method? Would any change in the legal and economic environment in which an investor operates still be permissible? In view of the arbitrators' inclination to answer such questions in favour of the investor, the concern over their interpretations is certainly well founded.

Second, many of the proposals being touted by the Commission as innovations can already be found in existing treaties or are already applied by arbitral institutions such as the ICSID – for instance, the intended and rather vague code of conduct for arbitrators and rules that allow abusive actions without any legal basis to be rejected in a simplified procedure. It is unlikely that these rules will put an end to the thriving business in combatting policies through investor-state lawsuits – to date they have not managed to do so either.

Third, with the exception of the transparency of the procedure, the »constitutional perversion« (Prantl 2014) that private arbitration represents is not even broached by the Commission. Hearings and requests for arbitration, as well as other essential documents, are supposed to be published in future; but instead of equality before the law, there are still special rights and special courts for investors. Their parallel legal system remains one-sided, because the Commission's proposals do not contain obligations on investors, for example, to respect labour rights.[16] Affected third parties will still not have legal standing in the proceedings,[17] and there will still be no

14. See the overview of the bilateral investment promotion and protection agreements (IFV) of the Federal Republic of Germany: http://www.bmwi.de/BMWi/Redaktion/PDF/B/bilaterale-investitionsfoerderungs-und-schutzvertraege-IFV,property=pdf,bereich=bmwi,sprache=de,rwb=true.pdf.

15. For a detailed and critical analysis of the Commission's reform proposals, see IISD (2014), Krajewski (2014) and Corporate Europe Observatory (2014: Annex 1 and 2).

16. According to the Commission's proposals, an investor would indeed forfeit the right to file lawsuits if investment has been made in a corrupt manner, but this is not the same as a duty to prevent corruption.

17. Although, according to the plans of the Commission, NGOs or trade unions are supposed be able to submit their own opinions to the proceedings (so-called *amicus curiae* submissions), this is not the same thing as the right to intervene in and even to become a party to the dispute – for example, in the case of an affected municipality whose measure is being reviewed in an investor-state lawsuit.

institutional safeguards to guarantee the independence of the arbitrators, who will continue to be appointed by the parties and to be paid per procedure in future.[18] And appeal proceedings before independent courts are not envisaged in the foreseeable future.[19]

Therefore, the Commission's reform proposals do not substantiate the promised new start in international investment law. Instead they involve marginal »mini-reforms« intended to re-legitimise the increasingly contested global legal field without touching the hard core of corporate privileges. The »reformed« investment protection à la the European Commission will also grant foreign investors more extensive private property rights than those contained, for example, in the German constitution. In addition, they will continue to have access to an exclusive corporate-friendly parallel legal system, in the form of private arbitration, to enforce these rights. Therefore, future EU investment agreements would also be part of the new constitutionalism that disciplines governments and places restriction on counter-hegemonic actors and redistribution processes.

Therefore, it is no surprise that even traditional hardliners on investment protection have overcome their initial scepticism to endorse the Commission's agenda. The recent position paper of the Federation of German Industries (BDI 2014), for example, is almost indistinguishable from the proposals of the EU bureaucracy.

When it comes to the central open questions concerning investment arbitration, however, neither the European Commission nor its friends from the BDI provide answers: Why should we grant tribunals composed of three private persons, which violate fundamental constitutional principles, the power to circumvent our legal system and review all laws enacted by our parliaments, all decisions of our governments and all verdicts of our courts, and to impose high compensation payments? And why should we grant a single group in our society – foreign investors – the power to take actions before these tribunals, and thereby to expand their power in the political process, without even a mention of imposing duties on them?

18. Although the Commission has announced a code of conduct for the arbitrators in future, such a code should not be confused with institutional guarantees of judicial independence, such as tenure for judges which prevents the less agreeable among them from being suspended.

19. The EU Commission has indeed announced that it wants to work towards an appeals mechanism, but such declarations of intention have existed in US contracts for years – without having led to such a mechanism. In the negotiations, the United States has already expressed scepticism regarding this proposal towards the EU.

5. What Should be Done?

The support of the business lobby for the Commission's reform agenda already indicates that it probably does not point the way to a socially just, environmentally sustainable and democratic investment policy. Those who are concerned about this should not let themselves be distracted by the »mini-reform« proposals. Nevertheless, the current politicisation of the topic in the EU presents opportunities for a genuine fresh start in investment policy along the following lines:

- Future investment agreements should neither include the unilateral dispute settlement nor go beyond the rights of private property conferred by the protection of property enshrined in national constitutions.

- Moreover, they should stipulate binding obligations on investors, such as duties to respect human and workers' rights, to protect the environment and climate and to pay taxes in the host country.

- Existing treaties should be cancelled or renegotiated so they do not restrict the regulatory autonomy of the state and neither contradict human nor workers' rights nor other societal goals such as sustainable development, nor violate constitutional principles.

As it happens, even then foreign investors would be far from defenceless. Today already, they have instruments for insuring themselves against political risks abroad, ranging from market-based private insurance, through the public insurance provided by the Multilateral Investment Guarantee Agency (MIGA), to agreements that individual investors can conclude with the host country. Joint ventures with companies from the host country or financing through loans from local banks also significantly reduce the risk of being arbitrarily expropriated by the host country.

The fractures in the global investment regime, which are currently being exacerbated, offer many starting points for a genuine fresh start in investment policy. The history of opposition to free trade and investment agreements has also shown that these anti-democratic neoliberal straitjackets can be prevented if the texts negotiated in secret can be made public and politicised. Thus, in the late 1990s the anti-globalization movement dragged the largely unknown Multilateral Agreement on Investment (MAI) – an investment agreement that had been negotiated within the framework of the OECD – into the public spotlight. Like a vampire, it did not survive long once caught in the rays of critical public debate. In October 1998, France put a stop to the negotiations. Forces for emancipation in Europe should do their utmost to ensure that this part of the story repeats itself in the controversy over the TTIP – and also in the case of all of the other planned corporate constitutions currently being negotiated by the EU.

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