Friends of the Earth Europe

The TTIP of the anti-democracy iceberg

The risks of including investor-to-state dispute settlement in transatlantic trade talks

October 2013

Introduction

"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." Juan Fernández-Armesto, arbitrator from Spain. [1]

Negotiations between the European Union (EU) and the United States (US) on a transatlantic trade deal – the Transatlantic Trade and Investment Partnership (TTIP) or the Transatlantic Free Trade Agreement (TAFTA) – started in July 2013. Decision-makers on both sides of the Atlantic have repeated that 'regulatory convergence' should be the main focus of the negotiations: tackling 'regulatory obstacles to trade' is promoted as a way of resolving current economic and financial crises, supposedly because it will boost growth and create jobs.

Friends of the Earth Europe believes that such aims and claims are worrying because such a 'convergence' is likely to challenge long-established environmental, health and consumer rights and regulations protecting citizens on both sides of the Atlantic as if they were burdens. The suggestion is that these should be sacrificed for (yet unproven and contested) economic benefits.[2] In that regard, one of the biggest threats looming over states' sovereign right to regulate could well come from the obscure 'investor-to-state dispute settlement mechanism' – also known, even more untransparently, as 'ISDS'.

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[1] www.globalarbitrationreview.com/journal/article/30399/stockholm-arbitrator-counsel-double-hat-syndrome
[2] http://trade.ec.europa.eu/doclib/docs/2012/april/tradoc_149331.pdf

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What is investor-to-state dispute settlement (ISDS)?

Specific investor-to-state dispute settlement (ISDS) provisions negotiated as part of free trade agreements (FTAs) or bilateral investment treaties (BITs) empower foreign investors to challenge national authorities in international courts, in order to claim financial compensation if they deem that their investment potential (and related profits) are being hindered by regulatory or policy changes that have occur at the national level.

Famous cases include attempts by Vattenfall to reverse Germany's decision to shut down its nuclear plants, Lone Pine attacking Québec's fracking ban, oil and gas giant Chevron evading compliance with its legal obligation to clean up the health and environment damages resulting from its operations in Ecuador, and Philip Morris challenging tobacco regulations in Australia and Uruguay.[3] Claims are handled in secret and unaccountable arbitration tribunals, bypassing the national court system.[4] Requests for compensation can amount to billions of dollars and represent significant burdens on states' public finances. In other words, ISDS allows corporations to question the sovereign right to regulate (whether or not it is in the public interest) based on their own commercial interests; it also leaves states powerless to stop claims and forced to pay the costs.

When it comes to environmental, energy, and public health matters, powerful transnational companies associated with environmental crimes and human rights abuses – such as Chevron or Occidental [5] - have been using this mechanism to maximise operating profits at the same time as undermining the regulatory frameworks they have to deal with abroad. In developing and developed countries alike, ISDS has been very useful for companies seeking to reverse regulations that protect the environment and people at the expense of corporate profits.

The real costs of ISDS:

According to UNCTAD:[6]

- **514 treaty-based cases were known about in 2012 – of which 58 new cases were initiated in that year.** This is the highest number of known disputes ever filed in one year, confirming that foreign investors are increasingly resorting to investor-state arbitration.
- **95 countries** had to 'respond' to one or more cases in 2012.
- **US and EU investors have initiated at least 329 (64%) of all known disputes**. For example, 123 of the 514 cases known about at the end of 2012 originated from companies based in the US; 50 from the Netherlands; 30 from the UK; and 27 from Germany.
- **Investors' claims were accepted in 70% of the known arbitral decisions about specific cases in 2012**. Nine cases awarded damages to the claimant, including the highest award in the history of ISDS with Occidental being awarded compensation of US$ 1.77 billion as a result of its claim against Ecuador.
- Out of all the concluded cases, **investors won outright in 31% of the cases and states won in 42%.** However, the rest of the cases were 'settled', meaning that the final decisions were generally not made public.
- The independence and impartiality of arbitrators ruling in ISDS cases, including the potential for

[3] See box with examples page 6
[4] For more information about the arbitration system, read: http://www.tni.org/briefing/profiting-injustice ; http://www.tni.org/article/response-critics-profiting-injustice
[5] http://www.amnestyusa.org/our-work/issues/business-and-human-rights/oil-gas-and-mining-industries/chevron-corp
[6] http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d3_en.pdf

conflicts of interest, have often been questioned. This small group of individuals is dominated by private lawyers (60%),[7] who can and do switch roles between arbitrator and legal adviser for private clients, depending on the cases. Just **15 arbitrators**, almost all from Europe, the US or Canada, have **decided on 55% of all known disputes** based on investment treaties. In 2011 just three international law firms were involved in 130 investment treaty cases – these were Freshfields (UK), White & Case (US) and King & Spalding (US).[8]

- The **average legal and arbitration costs** per ISDS case are estimated to be around **US$ 8 million.**[9] These costs cannot be recovered even when the other party loses the case; they therefore have to be paid with taxpayers' money. This also means that some countries — especially developing countries — might avoid introducing socially or environmentally progressive measures if for fear of being challenged through ISDS, because they cannot risk having to pay such costs.

In practice, ISDS provisions are specifically designed to protect and promote corporate interests by enabling investors to:

- demand financial compensation for breach of a contract or agreement in spite of the domestic right to regulate;
- challenge 'indirect expropriation', when the potential profits of an investment may be reduced because of a regulatory change or other decisions by a public authority (this can include environmental permits, health restrictions on tobacco, bans on energy extraction or pesticides, etc.);
- override a decision made in a domestic court;
- take states to international courts, made up of a panel of commercial arbitrators. These tribunals operate in absolute secrecy, with no appeals process and no information being made available. The costs of such legal challenges can be extremely high by way of illustration, the legal costs incurred by Ecuador in its defence against Chevron have amounted to US$18 million.

[7] http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d3_en.pdf
[8] http://www.tni.org/sites/www.tni.org/files/download/profitingfrominjustice.pdf
[9] http://www.tni.org/sites/www.tni.org/files/download/profitingfrominjustice.pdf

Why ISDS should be kept out of the TTIP

*"**These provisions challenge a country's sovereignty by giving foreign companies the right to take a national government to an international court**," Craig Emerson, Australia's Trade Minister*[10]

The leaked EU mandate for negotiating the TTIP suggests that ISDS is intended to be included in the final agreement: *"The investment protection chapter should cover a broad range of investors and their investments, intellectual property rights included, whether the investment is made before or after the entry into force of the Agreement […] **the Agreement should aim to provide for an effective and state-of-the-art investor-to-state dispute settlement mechanism** providing for transparency, independence of arbitrators and predictability of the Agreement, including through the possibility of binding interpretation of the Agreement by the Parties. **State-to-State dispute settlement should be included, but should not interfere with the right of investors to have recourse to investor-to-state dispute settlement mechanisms**. It should provide for investors as wide a range of arbitration fora as available under the Member States' bilateral investment agreements."* [11](emphasis added)

It is very much to be feared that the inclusion of ISDS provisions in the TTIP could act as a significant regulatory deterrent or obstacle discouraging states that would otherwise have been keen on introducing regulations that prioritise the interests of people and the environment over foreign investors' rights. States might be discouraged by the prospect of potential lawsuits that would add unsustainable burdens to their public finances. This puts ISDS in direct conflict with the domestic right to regulate and the fundamental precautionary and polluter-pays principles that are enshrined in EU treaties.

Friends of the Earth Europe believes that ISDS provisions should not be included in the transatlantic agreement under negotiation, for the following reasons:

- Specific ISDS provisions are elevating investors to the status of sovereign states, while they are limiting the powers of states with respect to foreign companies operating in their countries. This creates a serious impediment in terms of states' duty to regulate in the interest of their citizens, and may also prevent them introducing measures restricting the power of investors in the public interest. It could have particularly detrimental impacts on climate and environmental ambitions.
- Cases based on ISDS provisions bypass existing judicial remedies in favour of secret and unaccountable dispute settlement mechanisms. As both the EU and the US have strong and well-functioning court systems, this is neither needed nor justified.
- ISDS mechanisms also violate the exclusive jurisdiction of the European Court of Justice, so it can be argued they are not compatible with EU Treaties.[12]
- ISDS is a one-way mechanism that is not fair to states, since only investors can initiate claims on their own terms; states are limited to making counter-claims. Furthermore, the system only covers commercial activities; claims relating to environment or human rights are excluded.[13]

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[10] http://rabble.ca/blogs/bloggers/council-canadians/2013/04/nafta-challenge-to-fracking-ban-reason-to-avoid-investor-st
[11] http://www.s2bnetwork.org/fileadmin/dateien/downloads/EU-TTIP-Mandate-from-bfmtv-June17-2013.pdf
[12] http://acta.ffii.org/?p=1870 ; (http://www.tni.org/sites/www.tni.org/files/download/briefing_on_intra-eu_bits_0.pdf)
[13] http://www.lse.ac.uk/collections/law/wps/WPS2011-08_Kryvoi.pdf

- ISDS gives excessive rights to investors with no matching rights to go to international courts for citizens and communities harmed or abused by investors' projects and products. The same players that are so keen on protecting investors' rights would usually argue against similar rights for citizens or affected communities.
- From an economic point of view, the use of ISDS creates a duplication of layers of judicial authorities and adds an extra burden on public budgets for states that need to pay for their own defence even if they win a case that has been brought against them by an investor.
- Several countries are currently re-considering their involvement in ISDS because of its significant negative impacts on state sovereignty. These include India, South Africa, Australia, Brazil and Norway.[14]

Climate and energy: ISDS could be used to prevent measures restricting oil exploration or banning shale gas extraction

Transnational companies engaged in extractive operations are enthusiastic users of this costly settlement system. 60 out of the 169 (37.5%) ISDS cases pending before the International Center for Settlement of International Disputes (ICSID) at the World Bank, relate to oil, mining or gas.[15]

The introduction of specific rights for investors in the context of TTIP is particularly critical in relation to energy and environment. The development of unconventional fuels, particularly shale gas, is currently fuelling intense controversy across Europe, with the oil and gas industry lobbying heavily for assurances with respect to their investments in risky technologies such as fracking.[16] It is clear that there is strong willingness on the US side to secure the best conditions for investors exploring Europe's unconventional fuels potential, including shale gas and tar sands.

However, unconventional fuels are one of the most pressing and acute threats with respect to the climate and our environment. Decisions taken by national or federal governments not to allow shale gas projects because of their environmental and health impacts could be directly challenged and jeopardised by transnational oil and gas companies. However, it is imperative that states remain fully able to regulate the exploration and exploitation of fossil fuels, free from the pressure from companies and investors (which would be increased by the introduction of ISDS).[17]

[14] http://www.bilaterals.org/spip.php?article21295
[15] http://www.ips-dc.org/reports/mining_for_profits_update2013
[16] http://corporateeurope.org/sites/default/files/shale_gas_lobby_final.pdf
[17] http://www.foeeurope.org/foee-unconventional-and-unwanted-the-case-against-shale-gas-sept2012 ; http://www.foeeurope.org/shale-gas-economic-myths-210513

Chevron: promoting investor-to-state dispute settlement in TTIP as a model for strengthening big business interests in other trade agreements

"*A TTIP with strong and comprehensive investment provisions could set the global standard for investment protection now and into the future. Not only should that standard apply to investments between parties of the United States and the European Union in each other's market. To truly operationalize this standard, Chevron urges that, once negotiated, it be extended over time to future trade, investment or other related agreements to move us toward a globally-consistent, strong and comprehensive standard for investment protection.*
[…]
Investor-state arbitration is a concept that is being challenged by some governments today as an unwarranted infringement on their sovereignty. In fact, these dispute settlement provisions ensure that neither side has the power to unduly influence determinations of law and fact by assuring access to a neutral forum for resolving disputes."[18]

Chevron's position on TTIP assumes that states and companies should be put on the same level, illustrating a complete disrespect for states' sovereign power to regulate companies' behaviour and their essential duties to protect the interests of their citizens over the profits of powerful transnational companies. Chevron's approach also underlines the fact that the inclusion of an ISDS in the TTIP would set a very strong precedent for its inclusion in other trade agreements including at the global level, making it a particularly important objective from a corporate perspective.

The impact that ISDS provisions can have on environmental and citizens' safeguards relates partly to the broad definition of 'investment' used. An investment can include regulatory permits and licences, procurement contracts, or concessions to use natural resources. Therefore states that restrict oil and gas drilling, impose pollution controls or technology bans, or plan to close coal-fired plants or introduce other measures could be subject to investors' claims.

Under ISDS these claims could override states' sovereign right to regulate to protect citizens from the dangerous effects of unconventional and other fossil fuels extraction.

Furthermore, as noted by Chevron, it is to be feared that agreement on ISDS in any transatlantic deal could be used as a benchmark for future trade agreements respectively signed by the US and the EU with third parties, and even in global trade agreements. This could expand a dangerous, unaccountable, and business-friendly dispute settlement system, blocking sovereign nations' ambitions on climate and energy. This could, for example, prevent or discourage the EU with respect to trade restrictions on imports of oil from tar sands.

"We can't let little countries screw around with big companies like this – Companies that have made big investments around the World", *Unnamed Chevron lobbyist, quoted by Michael Isikoff in Newsweek* [19]

[18] Chevron's comments on the Transatlantic Trade and Investment Partnership to the Office of the US Trade Representative, available at: http://www.regulations.gov/#!documentDetail;D=USTR-2013-0019-0054
[19] http://www.thedailybeast.com/newsweek/2008/07/25/a-16-billion-problem.html

Salutary stories: how ISDS has already been used to challenge legislation on land and water contamination, nuclear power, fracking and public health

Vattenfall vs Germany: In 2009, Swedish energy company Vattenfall started an ISDS procedure against Germany, based on the Energy Charter Treaty, an international agreement protecting investments in the energy sector. Vattenfall had engaged in the construction of a coal fired power plant in Hamburg-Moorburg, located on the Elbe river. When Hamburg's Environmental Authority issued a licence imposing quality standards for the waste waters released by the power plant, Vattenfall claimed that those standards made the investment project unviable. Using ISDS provisions, the company asked Germany for compensation totalling €1.4 billion. Vattenfall and the city of Hamburg eventually settled the case with an agreement that foresaw the issuing of a "modified water use permit", which lowered the environmental requirements previously set by the Hamburg Environmental Authority.

Vattenfall vs Germany II: In May 2012, Vattenfall initiated a second international arbitration under the Energy Charter Treaty, this time asking for financial compensation with respect to Germany's decision to immediately close its oldest nuclear power plants and gradually shut down the remaining ones by 2022. This decision was taken in response to public concerns about the health and environmental risks of nuclear energy that followed the Fukushima accident in Japan. According to press sources, the claim for compensation by Vattenfall could amount up to €3.7 billion.

Lone Pine vs Canada: Based on provisions of the North American Free Trade Agreement (NAFTA) between the US, Canada and Mexico, US company Lone Pine Resources Inc. is asking for financial compensation from Canada following Québec's introduction of a moratorium on fracking. The moratorium introduced in May 2013 responded to concerns about the environmental and health risks posed by the new extraction method. The claim by Lone Pine amounts up to US$ 250 million (€191 millions). The case is still pending.

Chevron vs Ecuador: After years of litigation in Ecuador's national courts, Ecuador's indigenous people and farmers won a historic victory over Chevron (the court ruling requested that Chevron pay back US$18 billion to clean up the contamination of land and water that resulted from its operations). The company then turned to the investor-state mechanism under the US-Ecuador Bilateral Investment Treaty to overturn the national judgement and evade compliance. That arbitration tribunal ordered the President of Ecuador to block enforcement of the previous court orders. Subsequent rulings repeated this demand, arguing that Ecuador had violated the treaty further by allowing plaintiffs to try to seize Chevron's assets through courts in Argentina, Brazil and Canada. These rulings set a dangerous precedent, allowing corporations to challenge the functions of a country's domestic court system and the decisions of its duly-appointed judges – and it could violate Ecuador's constitutional separation of powers.

Occidental vs Ecuador: Ecuador terminated the contract of an oil concession with Occidental after Occidental sold 40% of its production right to another company without complying with its obligation to seek governmental approval for doing so, as specified in the concession contract. Occidental then challenged the decision, again under the ISDS provisions in the US-Ecuador Bilateral Investment Treaty. This resulted in the highest compensation ever awarded to an investor (US$1.77 billion), and demonstrates the vast power that tribunals wield.

Pacific Rim Mining Corp vs El Salvador: After failing to complete the environmental protection steps required to obtain a mining permit in El Salvador's main watershed region, Canadian gold mining company Pacific Rim Mining Corp. reincorporated a Cayman island subsidiary in Nevada and then filed an investor-state suit against El Salvador under the Central American Free Trade Agreement (CAFTA). The company is now claiming several hundred million dollars in compensation for its 'lost profits', challenging El Salvador's national mining laws. As an imminent jurisdictional ruling drags out, violence and threats against local environmentalists in the region where Pacific Rim wants to run a cyanide-leach gold mine continue.

Philip Morris vs Uruguay: After having transferred its international headquarters from the US to Switzerland for legal reasons, tobacco giant Philip Morris initiated a case against Uruguay in 2010 under the Switzerland-

Uruguay bilateral investment treaty. In spite of the fact that this treaty stipulates that it shall not be used to challenge public health measures, Philip Morris has used the agreement's ISDS to challenge several provisions of the recent Uruguayan tobacco regulations. The company has questioned health warning requirements for tobacco packages (including the graphic and size requirements) as well as the provision that prohibits marketing more than one tobacco product under each brand. While the case is still pending, it is a good example of the use of investment rules and ISDS as part of a strategic drive to oppose restrictions on tobacco marketing.

Philip Morris vs Australia: In 2011, Philip Morris Asia used the ISDS mechanism in the bilateral investment treaty between Australia and Hong Kong to challenge Australia's newly introduced tobacco regulation (the Tobacco Plain Packaging Act 2011). The tobacco giant has claimed that the new legislation deprives it of the real value of its investments in Australia and that Australia is treating them in an unfair and inequitable way. Philip Morris has demanded that Australia be ordered to suspend the enforcement of the plain packaging legislation and provide the company with billions of dollars of financial compensations for the losses incurred. The case, which is still pending, could have detrimental impacts on regulatory efforts to curb the lethal effects of smoking well beyond Australia. For example, the EU, which is currently reviewing its framework to regulate tobacco, has so far based its proposals on the Australian model.

Recommendations

- **Friends of the Earth Europe calls on the European Commission, the European Parliament, the EU's member states and the US government to reject the inclusion of ISDS provisions in TTIP, and to reject any final deal including such provisions.**
- **The EU Council, European Commission, and European Parliament should not sign up to any intergovernmental agreements that might enable an investor to take states to court or arbitration in order to challenge laws that enforce environmental, health, social, and consumer protection policies and regulations.**
- **Citizens and communities that are affected or abused by companies and investors should have, at the minimum, the same rights as investors with respect to accessing international courts.**

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