The future of investment arbitration in the light of Opinion 1/17

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1. *Introduction*

Alternative dispute resolution (ADR) is constantly gaining ground, both at domestic and international level. New forms of dispute settlement with a mix of public and private components are emerging in fields where this was not the case until recent times, as some contributions to this Zoom-out have attempted to demonstrate.[1] In the field of investment law we have witnessed a somehow opposite trend. Traditionally, disputes in this field have been settled by means of arbitral tribunals established mostly on the basis of bilateral or multilateral investment agreements (IAs) under a variety of arbitration facilities, which are collectively referred to as investor-to-State dispute settlement (ISDS). Traditional ISDS presents many characteristics of ADR, starting from the strong role that private parties play in it (for example when it comes to the appointment of arbitrators). The practice has shown that the system has clear advantages but also undeniable disadvantages.[2] The prevailing opinion in recent years has been that the latter considerably outweigh the former, resulting in what has been termed the backlash against investment arbitration in a volume appeared a few years ago.[3] In this contribution, however, I will not dwell on the details of the crisis that has affected

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[1] See, in particular, the articles written by Barbara Warwas and Stefania Marassi.

[2] For an overview see R Dolzer, C Schreuer, *Principles of International Investment Law* (OUP 2012) 235-237.

[3] See M Waibel, A Kaushal, KH Chung, C Balchin (eds), *The Backlash Against Investment Arbitration. Perceptions and Reality* (Kluwer Law International 2010).

investment arbitration, nor will I engage in a discussion of whether that backlash is entirely justified.[4] My focus will be much more modest.

One of the most tangible consequences of this growing dissatisfaction towards investment arbitration is the launch on the part of the EU of a court-like system to settle investment disputes – the now famous investment court system (ICS) – as a replacement to old-fashioned ISDS. The ICS now features in all EU IAs, and has become the standard position of the EU when it comes to dispute settlement in this field.[5] Recently, the ICS has also received the green light of the European Court of Justice (ECJ),[6] raising doubts as to whether traditional ISDS has conclusively been sent to oblivion, at least in the EU.

From a political and policy perspective, it is undoubtful that there is a strong stance on the part of the EU and of its Member States against traditional ISDS. This article, however, will focus exclusively on the legal dimension, by examining whether the ECJ's decision should be read as meaning that investment arbitration is incompatible with the EU legal system. While it is clear that Opinion 1/17 means that the ICS is compatible with EU law, it remains to be seen whether the Court's finding allows an *a contrario* reading. Namely, whether it entails the incompatibility with EU law of traditional ISDS.[7] The analysis will start with a brief summary of the events and developments that preceded the creation of the ICS and eventually led to the current situation (Section 2), followed by an examination of the relevant parts of Opinion 1/17 (Section 3). This part will be followed by an appraisal of the possible legal implications of the decision (Section 4). Some conclusions will be offered in the closing section (Section 5) in the attempt to look beyond the boundaries of EU law.

[4] For what is worth, I have taken position in regard to some of these aspects in previous publications, to which the reader is therefore referred. See, in particular, L Pantaleo, 'Lights and Shadows of the TTIP Investment Court System' in L Pantaleo, W Douma, T Takács (eds), *Tiptoeing to TTIP: What Kind of Agreement to What Kind of Partnership?* (CLEER Paper 2016/1).

[5] The EU is the main proponent on the international plain of the so-called multilateral investment court (MIC), that the Commission has been authorized to negotiate in the context of UNCITRAL. See the text of the negotiating directives available here <www.data.consilium.europa.eu/doc/document/ST-12981-2017-ADD-1-DCL-1/en/pdf>.

[6] See Opinion 1/17 *EU-Canada CET Agreement* [2019] (ECJ, 30 April 2019).

[7] This question is not a merely theoretical one. As discussed in Section 4 of this contribution, the Union is currently a party to at least one international agreement featuring traditional ISDS, and more generally, the possibility of concluding similar agreements may arise in the future.

2. *The background: From the backlash against investment arbitration to the ICS and the MIC*

The events that led to the creation of the ICS are well known. After the fall of the Berlin wall there has been an explosion of bilateral investment treaties (BITs) and IAs in general, which has resulted, in turn, in an explosion of investment disputes.[8] A number of serious issues have emerged in the abundant arbitral case law that has been produced in the last two decades or so. In brief, they relate to a) a – real or imaginary – lack of predictability and consistency of arbitral awards,[9] b) recurring conflicts of interest on the part of arbitrators,[10] and c) the excessive duration and high costs of the proceedings.[11] The emergence of these issues, coupled with some despicable abuses of the rules perpetrated by investors,[12] have given rise to widespread dissatisfaction with the system. Hence, the so-called backlash against investment arbitration.

The discontent reached its apogee in the EU when negotiations for the Transatlantic Trade and Investment Partnership (TTIP) were launched. The prospect of concluding an agreement featuring traditional

[8] For a comprehensive account of the historical developments of international investment law and IAs see Dolzer, Schreuer (n 2) 4-12.

[9] On this matter, see Y Banifatemi, 'Consistency in the Interpretation of Substantive Investment Rules: is it Achievable?' in R Echandi, P Sauvé (eds), *Prospects in International Investment Law and Policy: World Trade Forum* (CUP 2013) 220.

[10] See A Reinisch, C Knahr, 'Conflict of Interest in International Investment Arbitration' in A Peters, L Handschin (eds), *Conflict of Interest in Global, Public and Corporate Governance* (CUP 2012) 103.

[11] This categorisation is not accidental. These three issues are in fact the same ones on which UNCITRAL Working Group III, which is responsible of the reform of ISDS at the international level, has been focusing since 2017. See 'Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-fourth session' (Vienna, 27 November–1 December 2017) UN Doc A/CN.9/930/Rev.1.

[12] The most (in)famous example is undoubtedly the claim brought by a giant of the tobacco industry against Australia in order to challenge the so-called 'plain packaging' law introduced by that country with a view to making tobacco products less appealing to consumers and therefore reduce the consumption and the resulting devastating impact on human health of such products. As is well known, Philip Morris perpetrated a flagrant abuse of rights by relocating its headquarters from Australia to Hong Kong for the sole purpose of activating the jurisdictional clause included in the Australia-Hong Kong BIT at a time when the dispute was already foreseeable (as acknowledged by the Arbitral Tribunal). See UNCITRAL Arbitral Tribunal, *Philip Morris Asia Limited v The Commonwealth of Australia*, Award on Jurisdiction and Admissibility PCA Case No 2012-12 (17 December 2015).

ISDS with the US – which is home to many multinational corporations whose ethical standards have often been subject to criticism – was met with severe opposition in the European public opinion. In order to overcome that opposition, the European Commission tabled the proposal for a permanently standing investment court in what back then was essentially a surprise move.[13] Even though the TTIP negotiations have sunk somewhere in the vast Atlantic Ocean, the idea of a permanently standing adjudicatory body survived the shipwreck. The blueprint used as a (failed) attempt to save the TTIP has later become the EU standard position when it comes to investment disputes.

So far, the Union has managed to convince most of its trading partners to include an ICS in their investment agreements.[14] What is more, the EU – supported by like-minded countries like Canada – imposed itself as the main driving force behind a (still ongoing and likely heading to a failure) international effort aimed at establishing a multilateral investment court (MIC) featuring an appellate body.[15] It is beyond the scope of this article to dwell on the detailed features of the ICS and of the proposed MIC.[16] For the purpose of our discussion, suffice it to say that these are highly institutionalised judicial mechanisms that have essentially done away with the typically commercial features of investment arbitration.

Some key features of the ICS have come under the scrutiny of the ECJ in Opinion 1/17, in which the Court has made statements that seem to cast doubts as to the compatibility with EU law of traditional ISDS. In

[13] More details about the context in which the ICS was first proposed by the Commission are provided by Pantaleo (n 4) 77-78.

[14] The ICS features in the EU-Canada Agreement (CETA), the EU-Singapore Agreement (EUSA), the EU-Vietnam Agreement, and the EU-Mexico Agreement. More negotiations are currently ongoing. See the overview provided at the following address <www.ec.europa.eu/trade/policy/countries-and-regions/negotiations-and-agreements/#_in-place>.

[15] For a comprehensive account of the positions taken by different States and international organisations in the debate concerning the ISDS reform currently taking place within UNCITRAL and beyond see A Roberts, 'Incremental, Systemic, and Paradigmatic Reform of Investor-State Arbitration' (2018) AJIL 410.

[16] For an analysis of the ICS the reader is referred to L Pantaleo, *The Participation of the EU in International Dispute Settlement. Lessons from EU Investment Agreements* (T.M.C. Asser Press 2019) 69-98; for an examination of the MIC see M Bungenberg, A Reinisch, *From Bilateral Arbitral Tribunals and Investment Courts to a Multilateral Investment Court: Options regarding the Institutionalization of Investor-state Dispute Settlement* (Springer 2018).

some passages of the Opinion, the ECJ has seemed to set the standard so high that traditional investment tribunals simply may not make the cut. In other words, by finding that the ICS established under CETA is compatible with EU law, the ECJ may have indirectly ruled out everything that is placed below that standard. If that is the case, this would effectively mean that the EU would be prevented from concluding an agreement featuring ISDS altogether, somewhat crystallising in legal terms the shift of paradigm that was decided at the political level, and with it the said backlash against investment arbitration. The next two Sections will examine whether such conclusion is effectively warranted.

3. *The ECJ's main findings*

Opinion 1/17 is a complex and relatively long decision in which a number of issues have been put to the ECJ by the requesting Member State. For the purpose of this paper, however, the issues relating to institutional EU law aspects are not relevant and will therefore not be examined.[17] The analysis that follows will only focus on the third point of law raised in the Opinion, where the key procedural features of the ICS as well as its nature are assessed against the applicable EU legal framework.

First and foremost, the ECJ took a somewhat ambiguous position in relation to the question concerning the nature of the ICS as a judicial or an arbitral body,[18] effectively washing its hands of the matter. The Court

[17] In particular, this applies to the first two issues examined by the ECJ, namely the compatibility of the ICS with the autonomy of the EU legal order, and the compatibility of the ICS with the general principle of equal treatment and with the requirement of effectiveness. See Opinion 1/17 paras 106-188.

[18] The debate concerning whether the ICS is an arbitral or a judicial body may seem one of those issues that are of some interest only to the (not so large after all) community of legal scholars. At closer scrutiny, however, one can easily realise that this issue may have major practical implications. The determination of the nature of the ICS may in fact have a significant impact on the possibility to enforce the decisions issued by the ICS outside the territorial scope of application of the treaty based on which the ICS is established. For if it is established that the ICS is not an arbitral tribunal, any attempts to enforce its decisions based on the 1959 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, and even more so on the ICSID Convention, will prove almost certainly entirely futile. For an in-depth discussion of this issue see A Reinisch, 'Will the EU's Proposal Concerning an Investment Court System for CETA and TTIP Lead to Enforceable Awards? – The Limits of Modifying the ICSID

based its reasoning on the rules concerning the composition of the ICS,[19] as well as on the Joint Interpretative Instrument annexed to CETA. According to this document, the ICS 'moves decisively away from the traditional approach of investment dispute resolution and establishes independent, impartial and permanent investment Tribunals, inspired by the principles of public judicial systems'.[20] Based on this, the ECJ found that there was no 'need to ascertain whether the Parties will formally classify those tribunals as "judicial bodies" or whether their Members … will be called "judges"'. However, the ECJ conceded that the ICS 'will, in essence, exercise judicial functions.'[21] Interestingly enough, the Court found confirmation of this in the admittedly compulsory nature of the ICS' jurisdiction. According to the ECJ, such 'jurisdiction is mandatory not only for the respondent … but also for the claimant investor',[22] as a consequence of the circumstance that CETA lacks direct effects.[23]

On this basis, the ECJ proceeded to assess the compatibility of the ICS with the requirements established in Article 47 of the Charter of Fundamental Rights.[24] In this part of the Opinion, the Court applied its well-established case law concerning the requirements of independence and impartiality of a judicial body in general.[25] Without going into too much detail, the ECJ came to a positive determination. It found that the ICS is compatible with the requirements of independence and impartiality because of a number of reasons, which can be summarised as follows:

Convention and the Nature of Investment Arbitration' (2016) J Intl Economic L 761; as well as C Titi, 'The European Union's Proposal for an International Investment Court: Significance, Innovations and Challenges Ahead' (2017) Transnational Dispute Management 1.

[19] See Opinion 1/17 para 194.

[20] ibid para 195.

[21] ibid para 197.

[22] ibid para 198. Of a different opinion on this matter is Reinisch (n 16) 767-768.

[23] As is well known, EU investment agreements such as CETA include a so-called no-direct effect clause. Art 30.6 CETA is an example thereof. For a discussion of this clause and its implications on the ICS decisions see AD Casteleiro, 'The Effects of International Dispute Settlement Decisions in EU Law' in M Cremona, A Thies, R Wessel (eds), *The European Union and International Dispute Settlement* (Hart 2017).

[24] Charter of Fundamental Rights of the European Union [2016] OJ C202/389.

[25] See, *ex plurimis*, Case C-506/04 *Graham J. Wilson v Ordre des avocats du barreau de Luxembourg* [2006] ECR I-08613 paras 49 ff; Case C-64/16 *Associação Sindical dos Juízes portugueses* [2018] (ECJ, 27 February 2018) paras 43 ff; Case C-216/18 PPU *LM* [2018] (ECJ, 25 July 2018) paras 63 ff; Case C-619/18 *Commission v Poland* [2019] (ECJ, 24 June 2019) paras 71 ff.

a) the Members of the ICS will be adequately remunerated, b) they will only be removable from their office in limited circumstances, such as in cases of conflict of interest, c) the rules concerning the appointment of the ICS Members are susceptible of guaranteeing their equidistance from the disputing parties, and d) the composition of the divisions that will hear single cases are sufficiently randomized and unpredictable to the Parties to the agreement.[26]

In short, the Court has emphasized precisely those features of the ICS that differentiate it from traditional ISDS. Save for the requirement mentioned by the Court under a) above, the latter does not seem to be able to meet the other requirements that make the former compatible with the standard of judicial independence and impartiality applicable in the EU. Hence the question: does this mean that traditional ISDS that does not possess these features has been ruled out by the ECJ? Or to put it differently, does traditional ISDS have to comply with the requirements of independence and impartiality as applicable in the EU legal order? The next Section will focus on this question.

4. *The implications of Opinion 1/17 on ISDS: An appraisal*

From the outset, and as already noted above, it should be emphasised that the Court has applied its well-established case law concerning judicial independence in the EU. It is worth noting that the Court came to this determination only after it had reached the conclusion that the ICS is an organ exercising judicial functions with mandatory jurisdiction over the disputes arising out of CETA. That means, in other words, that the ICS is not just the only remedy available under CETA, also in view of the lack of direct effects of this agreement. It is also the only judicial remedy available to any natural or legal persons claiming a breach of CETA provisions. This is usually not the case for traditional ISDS. Therefore, a direct extension of the ECJ's finding in Opinion 1/17 to traditional ISDS seems to be difficult to maintain.

The reasons supporting this point are numerous. Firstly, traditional ISDS is not the only legal remedy available to investors whose rights under an IA have allegedly been breached. In fact, investors usually have

[26] See Opinion 1/17 paras 223-244.

the option to choose between litigation before the domestic courts of the host state and an international arbitral tribunal.[27] This option does not exist under CETA. Secondly, and differently from the ICS, there is little doubt that ISDS cannot be regarded as a judicial remedy. Its arbitral nature, as opposed to judicial nature, is actually its salient attribute, given that it is only by virtue of this nature that arbitral awards can benefit of the already mentioned privileged enforcement system.[28] Put differently, the ICS was subject to the strict conditions required under Article 47 of the Charter because of its specific characteristics, that is because of its unique status as a hybrid body exercising judicial functions under CETA. In short, the findings of Opinion 1/17 do not seem to rule out the compatibility with the EU law of traditional ISDS simply because that decision does not seem to apply to it in full.

If the argument made above is correct, a number of implications can be identified. First and foremost, it would still be legally possible for the Union to sign up to a treaty that includes traditional ISDS. Even though there is a strong political willingness in the EU to do away with it to the extent possible, one cannot rule out that the Union may want to conclude an IA featuring a more traditional form of investment dispute settlement. As a matter of fact, the EU is currently a party to one such treaty, namely the Energy Charter Treaty (ECT). Although the Union has recently engaged in an attempt to modernize the ECT which admittedly includes a reform of the provisions concerning the settlement of disputes, there is no guarantee that the attempt will lead to the creation of a court-like mechanism.[29] From this perspective, the reading of Opinion 1/17 offered

[27] It should be noted that investors sometimes do not actually choose one between these options and instead bring multiple proceedings concerning the same dispute under different instruments. This (quite problematic) practice is usually referred to as parallel proceedings, which is somewhat of a vexed question in investment arbitration. For an overview see E Gaillard, 'Parallel Proceedings: Investment Arbitration' *Max Planck Encyclopedias of International Law* <https://opil-ouplaw-com.peacepalace.idm.oclc.org/view/10.1093/law-mpeipro/e3329.013.3329/law-mpeipro-e3329?rskey=imWrhD&result=1&prd=MPIL>.

[28] See above (n 16).

[29] In fairness, the mandate conferred to the Commission by the Council only marginally concerns the settlement of disputes and seems to be focused, on the contrary, on the reform of substantive standards of investment protection. When it comes to dispute settlement, there is a rather general commitment to 'strive to ensure that ongoing multilateral reforms of investor-to-state dispute settlement, such as those within UNCITRAL WG III and ICSID, will be applied to the ECT. This includes striving to ensure that a future Multilateral Investment Court applies to the ECT'. See Council of

in these pages would not make the Union's continued participation to the system established under the ECT illegal under EU law.

A different reasoning applies to the MIC. At the time of writing, it is unclear what will be achieved exactly through the negotiations taking place in the relevant UNCITRAL Working Group. The EU is currently pushing for the creation of a standing mechanism for the settlement of investment disputes featuring two levels of adjudication, which is largely reminiscent of the ICS in many respects (including those scrutinized and approved by the ECJ in Opinion 1/17).[30] Given the variety of positions maintained by the States taking part in those negotiations, it is quite unlikely that the final outcome will be in line with the Union's *desiderata*. If the interpretation of Opinion 1/17 offered above is correct, this might very well mean that a watered down version of the MIC that does not meet the high standards of independence and impartiality applied by the ECJ to the ICS may result in its incompatibility with EU law. Unless it is designed so as not to constitute a judicial body altogether – or, to borrow from the ECJ, a (hybrid) body exercising judicial functions.

An implicit indication of this might actually be included in the ECJ's own words. The Court has repeatedly referred to the MIC in Opinion 1/17. As I have argued elsewhere, in those passages where the MIC is mentioned it seems to emerge the ECJ's intention to extend the findings applicable to CETA's ICS to the MIC as well.[31] This is somewhat explicitly stated in a sentence where the Luxembourg Court concluded that EU law does not preclude 'the creation of a Tribunal, an Appellate Tribunal and, subsequently, a multilateral investment Tribunal'.[32] From this

the European Union, Negotiating Directives for the Modernisation of the Energy Charter Treaty, 10745/19 ADD 1, 5. This appears to be in line with the agreement reached during the Ministerial Conference of the ECT in November 2018, where a list of items potentially subject to reform was approved. See Energy Charter Secretariat, CCDEC 2018 18 STR, available here <www.energycharter.org/fileadmin/DocumentsMedia/CCDECS/2018/CCDEC201818_-_STR_Modernisation_of_the_Energy_Charter_Treaty.pdf>.

[30] The main details of the mechanism proposed by the Union are summarized in the submissions made by it at UNCITRAL level. See United Nations Commission on International Trade Law, Working Group III (Investor-State Dispute Settlement Reform), Thirty-seventh session, New York, 1–5 April 2019, *Possible reform of investor-State dispute settlement (ISDS) Submission from the European Union and its Member States*, UN Doc A/CN.9/WG.III/WP.159/Add.1, 4 ff.

[31] See L Pantaleo, 'The Autonomy of the EU Legal Order and International Dispute Settlement in the Wake of Opinion 1/17' (2019) Studi sull'Integrazione Europea 793.

[32] See Opinion 1/17 para 118.

perspective, it is reasonable to assume that the ECJ has intended to give a signal that should be understood against the wider background and context that surround it.[33]

5. *Conclusions: Broadening the horizons*

The main argument made in this article could be summarized as follows. Opinion 1/17 should not be interpreted as meaning that a court-like system is the only option for the participation of the EU to the settlement of investment disputes. ISDS may still be permissible under EU law, provided it preserves the original features of traditional arbitration, starting from the voluntary nature of its jurisdiction as traditionally understood in international investment law.[34] Yet, if a court-like system is indeed created, the requirements of Article 47 of the Charter as interpreted in Opinion 1/17 and in previous case law are applicable. Given that the threshold is quite high, it will not be easy for such a court-like system to comply with those requirements.

From a more general perspective, this conclusion seems to leave a number of possible scenarios open. At UNCITRAL level, the Union is indeed promoting a court-like system that resembles closely the ICS it has adopted under bilateral IAs. However, it is endorsing in parallel the use of other forms of ADR such as mediation and conciliation,[35] which

[33] See also the opinion of E Kassoti and J Odermatt, who in their contribution to this Zoom-out argue that the ECJ's decision 'significantly bolsters the EU negotiating position in the context of the ongoing UNCITRAL negotiations on ISDS reforms'.

[34] As rightly pointed out by Bungenberg and Titi, however, the problem might lie with the substantive standards of IAs rather than with the procedural aspects of ISDS as opposed to the ICS. The ECJ has repeatedly stressed the importance of ensuring that litigation under CETA does not result in jeopardizing 'the level of protection of public interest' as established in the EU. This is, in essence, another way to refer to the need to safeguard the so-called right to regulate, which is heavily influenced by the way in which substantive standards are formulated. Yet, as rightly pointed out by these two scholars, 'a multilateral investment agreement on substantial standards is not in sight at this moment'. See M Bungenberg, C Titi, 'CETA Opinion – Setting Conditions for the Future of ISDS' EJIL:Talk! (5 June 2019) <www.ejiltalk.org/ceta-opinion-setting-conditions-for-the-future-of-isds/>.

[35] See, for example, the submission of the European Union to the relevant UNCITRAL Working Group, above note 30, where at para. 12 it is stated that '[i]t is desirable that disputes be decided amicably. Mechanisms should be provided to

are also included in all EU IAs. In general terms, these alternative forms of ADR seem to have the advantage of offering even more flexibility and autonomy to the disputing parties than investment arbitration. An intended or unintended – and perhaps slightly paradoxical – consequence of an increased judicialization of investment disputes may therefore result in the rise of even less formalized forms of ADR. Moreover, these alternative forms of ADR may also appeal to countries that have traditionally opposed investment arbitration and that do not seem to be willing to embrace a court-like system such as the ICS.[36]

encourage such amicable settlements. These could include, for instance, conciliation and mediation. Particular value–added could be brought through the provision of institutional support, for example through maintaining a list of conciliators or mediators and above all providing support in efforts to bring about amicable settlements'.

[36] These are countries like Brazil and South Africa, which have been supporting mediation and would possibly support the creation of an Ombudsperson for disputes involving foreign investors. See Roberts (n 15) 417.