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S&D Position Paper on Investor-state dispute settlement mechanisms in ongoing trade negotiations

The S&D Group opposes the inclusion of ISDS in Trade Agreements in which other options to enforce investment protection are available, whether domestic or international. In agreements with countries that have fully functioning legal systems and in which no risks of political interference in the judiciary or denial of justice have been identified, ISDS is not necessary.

The S&D Group strongly supports the principle that **foreign and domestic investors should be treated equally and fairly** and that this should be underpinned by substantive provisions on investment protection in trade agreements. Procedural provisions on investment protection - such as ISDS - should however always be context dependent and adapted to best fit the specific predicaments of the parties to an agreement. It is not reconcilable with the rule of law, that investors get a legal forum outside well-functioning judicial systems of the parties through a trade agreement. Investor protection provisions should apply to protection against discrimination, against expropriation without compensation and for the guarantee of fair and equitable treatment along well-defined and limited parameters. At the same time we firmly maintain the position that these provisions **must not in any way undermine the right to regulate in the public interest** as the Parties to the agreement see fit. We strongly support the establishment at multilateral level of an investment protection regime that finds a balance between these two principles.

The volume of foreign direct investment (FDI) has increased considerably worldwide over the last decades and has become a key factor for economic growth and jobs. The bilateral investment flows between the European Union and the United States alone total over 3,000 billion Euros, which represent an amount that far exceeds the FDI stock currently subject to the Member States' 9 bilateral investment treaties (BIT) with the US. Amongst countries with similar levels of investment protection in domestic legislation, there is no evidence that investment agreements - with or without ISDS - have any impact on investment flows.

Recently, the Investor-State Dispute Settlement Mechanism (ISDS) has brought a lot of public attention to EU trade policy with widespread concerns, in particular as regards its possible inclusion in trade deals with Canada (CETA) and the United States (TTIP). ISDS is not new and

neither is it an invention by the EU. Before the EU gained exclusive competence on investment negotiations with the Lisbon Treaty, Member States had already concluded more than 1,200 bilateral investment treaties (BIT) with third countries, a large majority of which contain ISDS. However the bulk of these investment treaties were negotiated with developing countries. As the S&D Group **we welcome the public attention and scrutiny the question of investment protection in EU trade agreements has garnered** as it illustrates the need for a broad debate which did not take place when previous BITs were concluded. We consider this a vital contribution to **reinforce the democratic legitimacy of the EU's trade policy**. In its report of 2011 on investment policy, the European Parliament pressed for the need to reform ISDS in light of its apparent substantial and procedural flaws.

We have observed in recent years a continued rise of ISDS cases, most of which were filed by EU companies with about a third of known cases decided in favour of the investor. Some of these have exploited the generic and vague drafting of previous investment treaties, which gives arbitrators large room for interpretation, to attack legitimate public policy objectives (e.g. Vattenfall vs. Germany related to Germany's renounce of nuclear energy, Veolia against Egypt on changes in labour law, Philip Morris against plain packaging in Australia, Lone Pine Resources Inc against Canada for a moratorium on shale gas exploitation. It should be noted that these cases have not been decided, yet, although regulatory chill effects have been felt already, for instance in New Zealand in relation to the Philip Morris case against Australia.)

The S&D Group has already on numerous occasions expressed its serious reservations concerning ISDS. In particular in the case of TTIP, we have made it clear that we do not see a need for its inclusion and have called for it to be excluded when negotiations for the investment chapter start.

Overall, the rule of law is sufficiently guaranteed among the US and the EU which calls into question the necessity of any arbitration mechanism parallel to national courts.

It is clear that well-founded concerns that the ISDS mechanism could be misused outweigh possible instances of discrimination against European investors. We regard a state-to-state dispute settlement system and the use of national courts as the most appropriate tools to provide investors with the fair opportunity to seek and achieve redress of grievances. The Council itself, has made it clear in its mandate for the Commission that ISDS is a desirable but not mandatory mechanism, and its inclusion is conditional on the overall balance in the agreement.

It should be noted that the ISDS in previous agreements is not necessarily equivalent to what is currently being negotiated by the Commission. The draft text of the CETA agreement, which is not, yet, ratified and is currently undergoing modifications in legal scrubbing, contains some improvement. This applies in particular as regards

- increased transparency as it relates to availability of documents and the public nature of hearings and rulings of arbitration,
- the introduction of a code of conduct for arbitrators which are controlled via the CETA Trade Committee,
- the more precise and clearer legal definitions on investment and indirect expropriation,
- the necessity for substantial business operations in the territory of a host state which prevent the use of shell companies to benefit from ISDS provisions in otherwise not applicable treaties,

- the mentioning of the right to regulate in the public interest in the preamble of the agreement,
- the ruling out of loss of anticipated future profits for initiating a case
- the possibility for parties to the agreement to issue binding interpretative definitions of provisions in the investment chapter to rule out unintended consequences in the aftermath,
- the introduction of state-to-state filters to prevent cases in the financial and tax sector.

For CETA the situation is different compared to TTIP as the negotiations have been concluded already. Nevertheless, we stress that these reforms are clearly insufficient to close the loopholes. This is also underpinned by the fact that the Commission's online public consultation on ISDS in TTIP, which had the CETA text as a reference document, between 27 March and 13 July 2014 garnered an unprecedented number of replies with nearly 150,000 coming from all 28 EU Member States. 97% of these responses showed a widespread opposition to ISDS in its current form which illustrates the great concerns widely held among the public about this issue. The consultation notably highlighted widespread concern that a) ISDS in its current form limits public policy space, creating a risk of "regulatory chill", b) ISDS discriminates domestic investors.

We take these concerns by the public very seriously and believe that there cannot be any business as usual after this consultation. We will fight to have the citizens' widespread concerns addressed in these trade negotiations.

In its report on the public consultation the Commission identified the following four areas in particular for exploration of further improvements: **the protection of the right to regulate, the establishment and functioning of arbitral tribunals; the relationship between domestic judicial systems and ISDS, and the review of ISDS decisions through an appellate mechanism.** The Commission has, thus, at least recognized that there are serious shortfalls in the current ISDS regime but has so far not presented any solutions, whereas, these areas of concern were largely already identified by the Parliament and the S&D Group in the investment report of 2011.

We consider the present debate an opportunity to form an investment policy which promotes productive, sustainable and decent jobs creating investments, respects the environment, encourages good quality working conditions and makes a positive contribution to worldwide economic growth and sustainable development, particularly given the far-reaching extraterritorial effects a successful conclusion of TTIP would have. In an era of increased inward investment as compared to when the early BITs were concluded it becomes increasingly important to consider the domestic effects of investment protection rules and, given the apparent shortcomings of the current ISDS regime, it is important that a thorough review of possibilities for reform is conducted.

We are, therefore, against any rushed, methodologically unsound investor-to-state mechanism in TTIP to avoid any unintended consequences. One should also note that there are other means available to provide for investment protection both in the public and in the private sector, such as export credits and political risk insurance.

With regard to CETA, we welcome that some EU governments, led by S&D sister parties, are still trying to further improve the provisions on investment protection, as compared to what has been achieved already in ISDS reform. We support this process and reserve our final

judgment on CETA once the entire package is referred to the European Parliament for consent.

In trade agreements in which dispute settlement may be needed, we highlight specifically the following areas for potential further improvement:

- a clause enforcing the prohibition of parallel proceedings,
- a general political filter which allows parties to the agreement to block a claim from proceeding to ISDS arbitration,
- a clear and guaranteed path towards the establishment of an appeal mechanism,
- the guaranteed and full participation of the public in arbitration,
- a standing arbitration court with independent judges not subject to conflicts of interest and with mandatory rules on ethics,
- a clear and unambiguous clause which horizontally asserts the right to regulate in the public interest,
- a guarantee that nothing prevents a once outsourced service from being brought back into the public sector,
- a clear statement that non-discriminatory acts to protect legitimate policy objectives, such as social, environmental, security, stability of the financial system, public health and safety, do not constitute indirect expropriation,
- a "no greater rights"-clause which makes it clear that foreign investors should not have more rights than domestic ones,
- the exclusion of social and labour legislation from areas subject to ISDS arbitration ,
- a duty to exhaust the legal process before domestic courts before having recourse to ISDS arbitration ,
- the introduction of a revision clause which would enable parties to revisit their agreements to make sure it reflects evolving international best practice when it comes to investment protection, which would also reflect the character of a "living agreement" in TTIP
- an expanded state-to-state filter for sensitive policy areas such as consumer protection, public health and environment.

Furthermore, we reject any arguments that claim that ISDS must be accepted in TTIP right away as a precedent for future negotiations with other third countries. We judge all bilateral trade negotiations on their own merit.

We have an interest in a good TTIP that becomes a gold standard agreement. We do not want to see this opportunity jeopardized by the inclusion of provisions on ISDS which are not acceptable to the S&D Group, a majority in the European Parliament, and the general public.