



Investment in CETA – A response to a lobby document by DG Trade

The European Commission note on **“Investment Provisions in the EU-Canada free trade agreement”** is a **lobby document**, not an objective and complete presentation on the issue

By Marc Maes (11.11.11) for the Seattle to Brussels Network

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At the end of 2013 the European Commission produced a note presenting and explaining the “Investment Provisions in the EU-Canada free trade agreement” (CETA)ⁱ This note must be regarded as a lobby instrument to rally support in parliaments and public opinion, but it is definitely not a complete and objective presentation of where the negotiating texts really standⁱⁱ. The discrepancy between the Commission’s note and the texts (of which leaked full versions were seen by S2B) demonstrates once again that more transparency is needed and that only the texts themselves can give an objective picture of where negotiations stand.

CETA’s Investment Protections

The first part of the Commission note deals with the provisions of the investment protection chapter in CETA. In the introductory paragraph, the Commission claims, *The EU and Canada agreed to bring very significant clarifications to the key substantive provisions,* and that *“the arbitrators will now have strict and detailed guidance when these provisions are invoked by an investor.”* This is demonstrably incorrect, especially with respect to the open-ended Fair and Equitable Treatment (FET) standard, and the leeway it gives to arbitrators to determine the confines of acceptable regulation.

The Commission claims in its first point in this section that CETA reaffirms the right to regulate. This is not the case. The CETA investment chapter of 21 November 2013 does not contain a general paragraph reaffirming this right that would apply to the whole chapter. There is only such a paragraph in the annex on expropriation – an often problematic clause in investment treaties but one that is not as widely used to attack general policies as the FET standard.

A general paragraph on the right to regulate does appear in the preamble to the whole CETA text, which reads: *“RECOGNIZING the right to regulate within their territories, in a manner consistent with this Agreement, to achieve their public policy objectives.”* Quite clearly this formulation does not reaffirm the right to regulate. On the contrary it subjects all government regulation it to the terms of the agreement. The investor-state dispute settlement process allows private investors, who are not party to the agreement, test the legitimacy of this regulation through private arbitration, subverting the democratic process.

The Commission's second point on this issue claims that there is a precise definition of the FET standard in CETA. Again this is misleading when compared to the relevant section in the 21 November CETA text. The definition of FET given in the CETA text is of a hybrid form: it combines a more precise closed list of what would breach the treaty rights in some articles with open ended and vague formulations in others. The result is the opposite of clarity, leaving arbitrators in an investment tribunal far too much freedom to interpret these rights. The Commission does not address this contradiction. Instead, the note on the CETA investment text only presents the closed list of less controversial violations of an investor's rights, for example to be safe from manifest breaches of international legal norms, discrimination on racial grounds, etc.

Almost as a footnote, the Commission adds that an FET violation could occur under "*a breach of legitimate expectations*" but that this "*is limited to situations where the investments took place ONLY because of a promise made by the state that was subsequently not honoured.*" (Emphasis added.) This is not what the article in the 21 November CETA text says. The actual language is, "*when applying the above FET obligation a tribunal may take into account whether a Party made a specific representation to an investor to induce a covered investment, that created a legitimate expectation, and upon which the investor relied in deciding to make or maintain the covered investment, but that the Party subsequently frustrated.*" Note that this clause does not say that the investment only took place *because* of this representation, but it does leave such tricky questions completely up to the three arbitrators deciding the case. So the actual scope of the article is much broader than the Commission wants us to believe.

There is even more obfuscation in the Commission note on CETA. For example, there is no reference to language in the CETA investment that explains:

1- the Parties can every [...] years review (i.e. amend) the content of the FET obligation, to enlarge it for example;

2- in addition to the closed list of FET violations, a breach of the CETA investment chapter can also result from "*the FET obligation recognized in the general practice of States accepted as law.*" This is yet another vague formulation that leaves a lot of space for the arbitrators to make interpretations.

In item 5 of the Commission's third point on the CETA language on expropriation, the note states the obligation to provide "full protection and security" to investors does not cover protection against changes of laws and regulations. However, the 21 November CETA text does not say this with so many words, only that this obligation refers to the physical security of investors and covered investments.

In item 8 of the point on expropriation, the Commission says that CETA, like other EU Free Trade Agreements, permits the adoption and enforcement of prudential measures (e.g. measures taken to protect against systemic risk to the financial system). However these are limited to balance of payment problems and to "strictly necessary" measures that cannot exceed six months restricting transfers (of capital and payments) in case of serious difficulties for the operation of monetary or exchange rate policy.

CETA's Investor-State Dispute Settlement Process (ISDS)

The second part of the Commission's note on CETA relates to the investor-state dispute settlement process (ISDS) through which Canadian and EU companies will be able to directly challenge government measures as breaching CETA's substantial investment protection rules. As with the investment rules chapter, much of the actual CETA text is left out or else explained in a way that purposely hides the likely impacts of ISDS on European governance.

The Commission claims under point 4 here that CETA has introduced a binding code of conduct for arbitrators. However that code is not explained because it has not been developed yet but will be adopted by a joint (EU-Canada) committee within two years of CETA's entry into force or its provisional application. Worse is that the text says the arbitrators have to follow this code OR the International Bar Association Guidelines on Conflict of Interest in International Arbitration, which is a general code not geared to ISDS. This essentially means that the code is NOT binding.

Point 7 in the Commission explanation of ISDS says that all arbitration hearings and all documents will be open to the public. However, the 15 November CETA ISDS text foresees several exceptions to this openness, allowing arbitral tribunals to hold back confidential information in some cases and to take parts of hearings in private. Tribunals have the freedom to do this to protect the "integrity of the arbitral process," or "confidential business information," but also for vague "logistical reasons."

In the next point, the Commission boasts that CETA would for the first time create the possibility of establishing an appellate mechanism that could review arbitral awards and the tribunal's reasoning. One of the strongest critiques of ISDS is that unlike in most standard legal systems, the word of arbitration panels is final and binding. They can be wrong and yet they are always right under the rules of investment treaties like CETA. Unfortunately, there is no real commitment in the CETA ISDS text to create an appeals process – only suggestions that a "Committee on Services" may, if it so desires, consult on the possibility at some undetermined point in the future.

Under point 9 the Commission says that there are explicit provisions for mediation for investment disputes, before they reach the arbitration stage, but this is completely voluntary. The Commission then states that there is "absolute clarity" that a state cannot be forced to repeal a measure where that measure has been found by a tribunal to have breached an investor's rights under the CETA investment rules. The 15 November CETA text does indeed allow the arbitration tribunal to only impose monetary damages or restitution of property (which may also be replaced by monetary damages). However, as in past investment treaties, it is clear the threat of damages or the threat of facing an investor-state challenge may be enough for governments to repeal the disputed measures voluntarily, as has happened so often in out-of-court settlements between the investor and the targeted governments.

Finally, under point 11 in the ISDS section of its explanatory note, the Commission says that CETA foresees effective mechanisms for the Parties to the agreement to issue binding interpretations. These are meant to guide or restrict tribunals as they consider ISDS cases. However, such interpretations are only valid if they are made before the measures in dispute were taken. This means that such interpretations can only be made in response to an undesired arbitration award (i.e. after they have paid damages already) that the Parties do not want to see repeated again. The old saying "Hindsight is 20-20" is no comfort when ISDS awards frequently run into the hundreds of millions, if not billions, of Euros (without counting legal fees).

Other critical points in the texts not mentioned in the Commission's note

In addition to the elements addressed in the Commission's note on investment, there are other important critical remarks to be made about the CETA texts ⁱⁱⁱ:

1. In the investment protection chapter, the definition of investment is defined too broadly, covering any kind of asset, independent of whether or not investments are associated with an existing enterprise in the host state.
2. The investment protection chapter contains a "most favoured nation" (MFN) clause which will allow foreign investors to invoke any rights given to investors from other countries, including rights given under other investment treaties. This will nullify any new element or formulation, "reforms" or "modernisation" that the CETA text may contain as investors will be allowed to use the provisions and the language of other investment treaties that Canada or the EU have ratified instead! To a certain extent the EU is aware of this problem as it has excluded the market access provisions and the investor-state procedures of the investment chapter from the scope of the MFN clause. This will not however prevent investors from invoking other elements in older investment treaties, especially the way investment protection standards have been formulated.
3. The text contains a (bracketed) umbrella clause that is absent in Canadian BITs and would substantially broaden the scope of the treaty. Umbrella clauses make it possible for investors to take breaches of a contract or of other commitments made by the authorities of the host state to the investor to investment arbitration as if it were a violation of the treaty itself..
4. The text contains a "survival" clause which extends the applicability of its investment provisions 20 years after the termination of the agreement for investments that were made before the date of termination.
5. The text contains a long article on general exceptions (e.g. with regard to privacy, health) but they are vague and the Commission wants to limit the exceptions to market access so that they do not apply to the investment protection standards or national or MFN treatment. We should also question the effectiveness of introducing GATT-style general exceptions clause into the investment protection chapter. WTO tribunals have already interpreted these exceptions very narrowly and against a "necessity test" that sees regulation as a measure of last resort. Giving arbitration panels a green light to apply a necessity test to investment measures dangerously subverts the democratic process.
6. In the ISDS chapter the Commission has introduced the possibility of arbitration with one arbitrator for small- and medium-sized enterprises, or when the damages claimed are low. This will lead to increased litigation as it will make ISDS less costly and more accessible.
7. The chapter foresees wide competences for a joint "Committee on Services and Investment" so that it can – after completion of the respective legal requirements and procedures of the Parties –adopt and propose amendments, rules, interpretations, etc. This is intended to make CETA a "live" agreement that can be adapted to circumstances. This raises the question of how parliaments, civil society and the general public will be able to scrutinise the continuous expansion of the agreement.

CONCLUSION: Let us not lose sight of the forest behind the trees

There is more to the investment provisions and ISDS chapters in CETA than the European Commission wants the public to see. Moreover, despite all the small or larger reforms that are being introduced in the Canadian treaty compared to EU member state BITS, the investor-state arbitration system that CETA would establish is far inferior to the domestic legal system of the EU and North America.

ISDS is precisely and only meant to allow foreign companies to have greater rights than domestic companies and citizens, and to disregard domestic laws if they feel these have breached their substantial “rights” in a given investment treaty. CETA and later the EU-US Transatlantic Trade and Investment Partnership (TTIP) will forever surrender, to paid arbitrators, the judgement over what policies are right or wrong, legitimate or illegitimate. The sheer volume of North Atlantic investment that will be covered by these treaties will guarantee a large number of cases for these arbitrators to decide. This should not be allowed to happen.

i See: http://trade.ec.europa.eu/doclib/docs/2013/november/tradoc_151918.pdf

ii The most recent texts sent by the European Commission to the Member States date from 15 November (for the ISDS part) and 21 November (for the rest of the Investment chapter). The latter was redistributed among the member states on 7 January 2014.

iii See also Nathalie Bernasconi, *The Draft Investment Chapter of the Canada-EU Comprehensive Economic and Trade Agreement: A Step Backwards for the EU and Canada?* IISD, 26 June 2013. http://www.iisd.org/pdf/2013/iisd_itn_june_2013_en.pdf; and Howard Mann, *Submission to the Canadian House of Commons Standing Committee on International Trade*, 5 December 2013 http://www.iisd.org/pdf/2013/CIIT_final_submission_trade.pdf