

Investor-State Arbitration and the Rule of Law: Debunking the Myths

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Acronyms

ALP	Australian Labor Party
ASEAN	Association of Southeast Asian Nations (Indonesia, Malaysia, Philippines, Singapore, Thailand, Brunei, Vietnam, Laos, Myanmar and Cambodia)
AUSFTA	Australia-United States Free Trade Agreement
BIT	Bilateral Investment Treaty
EU	European Union
FTA	Free Trade Agreement
ICSID	International Centre for Settlement of Investment Disputes
IIA	International Investment Agreement
ISDS	Investor-State Dispute Settlement
PC	Australian Government's Productivity Commission
SAFTA	Singapore-Australia Free Trade Agreement
TPP	Trans-Pacific Partnership (Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, Peru, New Zealand, Singapore, the United States and Vietnam)
UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
US	United States of America
WTO	World Trade Organisation

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Any errors or omissions in this research report remain the author's responsibility.



Executive Summary

- Investor-State Dispute Settlement (ISDS) is a legal provision in international agreements that enables foreign investors to take host states to an arbitral tribunal for alleged treaty breaches.
- The goal of investor-state arbitration is to provide a de-politicised, unbiased and law-based adjudication forum to guarantee the investor's rights against unlawful overseas government actions.
- First and foremost, the case for investor-state arbitration lies in the strengthening of the rule of law — the quintessential feature of free markets and individual liberty, and indeed a cornerstone to human prosperity since Magna Carta.
- The first ISDS agreement was signed in 1959 between Germany and Pakistan. Since then, investment-protected international treaties have been gaining pace worldwide, from less than 500 agreements in 1990 to 2184 in 2000 to 3509 at the start of 2016.
- Likewise, as globalised capital flows and international investment agreements proliferate, ISDS cases have accelerated since the turn of the millennium. From close to 100 proceedings initiated before 2003, the total amount of known ISDS cases are currently at 608.
- Although most ISDS claims are brought against non-developed governments, the share of developed states responding in investor-state arbitrations is lately on the rise, currently accounting for almost a third of all cases.
- Of the total 362 currently concluded ISDS cases, only 30% of rulings have been in favour of foreign investors, with the great majority ruled either in favour of the state or consensual settlement among the disputing parties.
- Australia has agreed to ISDS protection in 21 bilateral investment treaties and seven free trade agreements. However, support for ISDS provisions in Australia has swung from full engagement in the 1990s to outright rejection during the Gillard administration, to the current 'case-by-case basis' approach.
- In the past 30 years since Australia's first ISDS-protected treaty, the world has become a safer place for Australian investors, with investor-state arbitration acting as a powerful and effective Sword of Damocles against unlawful foreign government acts — and in three occasions indeed providing a neutral and de-politicised forum to assert a just treatment to Australian interests overseas.
- Domestically, ISDS brings little disruption, given the high standards of Australia's rule of law culture: for example, the first and only ISDS case against the Australian government (on tobacco packaging legislation) has been recently dismissed.

- Investor-state arbitration has been in the spotlight in Australia due to the current parliamentary discussions on ratifying the Trans-Pacific Partnership, with detractors questioning the introduction of ISDS provisions in the agreement.
- This report recommends that Australia should fully embrace investor-state arbitration, including in the TPP agreement — given its transparent, well-delimited and legitimate use of ISDS provisions.
- Moreover, responding to valid concerns, Australia should maintain its international efforts to implement an ISDS appellate mechanism, and whenever possible, to work with its trading partners to ensure that previous ISDS commitments are updated and fit for purpose, given the latest advancements in the field.
- As part of an evidence-based and informed debate, this report debunks the seven major myths about investor-state arbitration:

Myth 1. ISDS breaches sovereign immunity

Investor-state arbitration is a conscious act of sovereignty, and there is nothing in its arrangements that cannot be separately found in other legitimate legal instruments and procedures.

Myth 2. ISDS tribunals can overturn national legislation

ISDS tribunals do not have the authority to reverse national legislation or regulations. If anything, investor-state arbitration constitutes an extra layer curbing government's ability to *misregulate*.

Myth 3. ISDS provisions give special rights to foreign investors

ISDS simply provides the necessary means to enforce international treaty-based agreements in accordance to the rule of law.

Further, there is nothing in ISDS material protections that is not covered — or should not be covered — by any nation that respects the rule of law.

Myth 4. ISDS provisions should not be part of international treaties among developed nations

ISDS provisions should be included in international treaties among developed nations, since a patchwork collection of ISDS-protected agreements is counterproductive and undermined by treaty shopping conduct.

Myth 5. ISDS is redundant in international affairs

ISDS is an effective and unique tool to overcome political risks. For example, political risk insurance and private contracts with host governments cannot fully substitute the benefits of investor-state arbitration.

Myth 6. There is no economic case for ISDS

The porous global rule of law constitutes a strong economic case for ISDS provisions to provide a safer environment for international investments.

Myth 7. ISDS benefits only big multinationals

ISDS benefits business of all shapes and sizes, with a greater part of claims initiated by either individual investors or small and medium enterprises.

- The takeaway message is that there is nothing to fear from investor-state arbitration and much to welcome it.



Introduction

With vast natural resources and a highly skilled population, Australia is well placed to benefit from global trade and investment flows.¹ Traditionally, foreign investments have filled the shortfall in our national savings, helping to finance current consumption levels and sustaining higher economic growth rates.² According to a recent study, for every 10% increase in foreign investments, Australia's annual production and wages increase respectively by 1.2% and 1.1% in real terms over a 10-year period.³ Australia is an attractive destination with a long track record of international capital inflows, and latest data shows the total stock value of foreign investment in the country amounts to \$2.8 trillion.⁴

Conversely, Australian businesses have also benefited from investing overseas, with the total value of outward investment more than \$1.9 trillion at the end of 2014.⁵ All these figures reinforce the traditional gains from trade and the importance of cross-border capital movements to Australia's national interest. Nonetheless, history has shown time and again that support for foreign investments in Australia has been shaky.⁶

A recent development in the global battle between free trade supporters and national protectionists — echoed in Australia — is the rise of Investor-State Dispute Settlement (ISDS) provisions in international agreements that allow foreign investors to take a host government to a neutral, third-party arbitral tribunal in the event their rights are infringed.

Prior to the introduction of ISDS, there were limited options for investors seeking recompense from unlawful acts of foreign governments. Some sought reparation in the host state's domestic courts, which at times proved to be a daunting enterprise due to corruption, partiality and idiosyncrasies of different national justice systems. Alternatively, others relied on their own national government's sponsorship to recover losses at the risk of an escalation to state-to-state conflict. Indeed, the latter practice occasionally led to the ill-reputed 'gunboat diplomacy', where powerful states would threaten to (or actually) militarily intervene in other sovereign nations in order to secure private commercial interests. For instance, from independence until World War II, the United States performed 88 military interventions in foreign countries to protect the interest of American private investors.⁷

Nonetheless, the truth is that before ISDS arrangements, the ability of private investors to effectively recover reparation from rogue foreign governments was meagre — by the United Nations' accounting, there were 875 illegitimate government appropriations of foreign investors' property spread over 62 different countries in the years following the end of World War II.⁸ This insecure global scenario unnecessarily increased the sovereign risks associated with international ventures, penalising both importers and exporters of capital.

In the midst of such a lawless international environment, the international legal option of accessing arbitral

tribunals to settle disputes between private investors and foreign governments presented an effective alternative as a neutral forum for a fair and de-politicised hearing. The first international agreement containing ISDS obligations was set out in the 1959 Bilateral Investment Treaty (BIT) between Germany and Pakistan.⁹ Since then, the number of investment-protected international agreements have been gaining pace worldwide, from less than 500 agreements in 1990 to 2184 in 2000 to 3509 at the start of 2016 (**Figure 1**).¹⁰

As ISDS became more and more pervasive in global affairs, there has been considerable clamour against investor-state arbitration. The democratic credentials of ISDS provisions have been questioned by critics, with claims that such a legal option constitutes an attack on sovereignty, undermining the national ability to conduct public policy as well as providing special rights to foreign investors.¹²

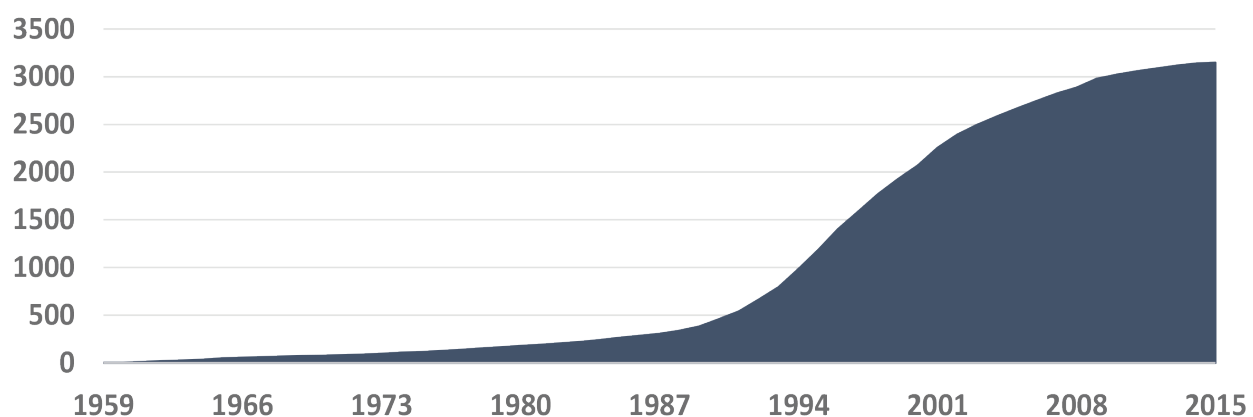
In Australia, the wave of criticism is identical: ISDS was once rejected by the Productivity Commission, providing ammunition for the Gillard government to temporarily cull it from international treaty negotiations.¹³

At the moment, investor-state arbitration is at the core of parliamentary discussions over the ratifications of the Trans-Pacific Partnership, with the Australian Greens calling it a “*Trojan Horse in our secretive trade agreements*”.¹⁴

ISDS provisions come in all shapes and sizes, varying in a wide range of topics such as: consent form (e.g. implicit or explicit); preferred ISDS forum facility; time limitations on notification and cooling-off periods; and scope restrictions — for instance exempting certain regulatory areas or even particular industries from arbitral disputes.¹⁵ In other words, one should think of ISDS as an ever-evolving class of legal instrument, with no ‘one size fits all’ arrangement.

This report examines the growth of investor-state arbitration provisions and cases worldwide and explores whether this legal institution suits our national interests: Should Australia embrace ISDS provisions in international agreements? Are propagated criticisms of investor-state arbitration myths or realities? What can be done to mitigate associated valid concerns?

Figure 1: Investment-Protected International Agreements



Source: UNCTAD; Author’s calculations.¹¹

Box 1: A Typical ISDS Proceeding

The life of an ISDS proceeding starts with an alleged misconduct by a government violating international investment treaty obligations, with most ISDS claims concerning administrative government acts with respect to land zoning, breaches of contract and cancellation of licenses and permits.¹⁶ In any case, it is up to the foreign investor to properly notify the government authorities and, when required, wait for the cooling-off period before starting the arbitral proceeding in an authorised ISDS forum facility.

Once the arbitral proceeding is initiated, the disputing parties need to agree on the *ad hoc* (i.e. appointed) arbitral tribunal selection. Usually, the investor claimant and the state respondent have the right to appoint one arbitrator each, with a third umpire either nominated by the arbitral facility or by mutual agreement among the disputing parties. As a general rule, appointed arbitrators must be qualified experts on the matters involved in the case, as well as being expected to adjudicate with impartiality and fairness.

Proceedings must follow the rules of the arbitral forum facility under which the ISDS claim is analysed. A great majority of ISDS cases are overseen either by the World Bank's ICSID forum¹⁷ (64% of all ISDS cases) or by United Nations' UNCITRAL¹⁸ rules (29%) — **Figure 2**. Nonetheless, despite a few procedural differences, all arbitral tribunals aim to provide an independent, depoliticised and effective dispute-settlement forum.¹⁹

On average, ISDS cases last approximately 3.5 years, with 29% of cases resolved by mutual settlement of the disputing parties — **Figure 3**.²⁰

Figure 2: Preferred ISDS Arbitration Forums

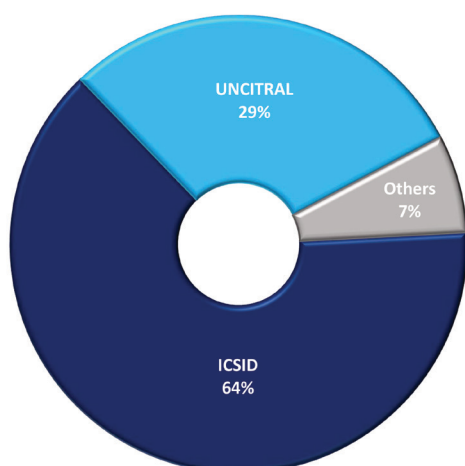
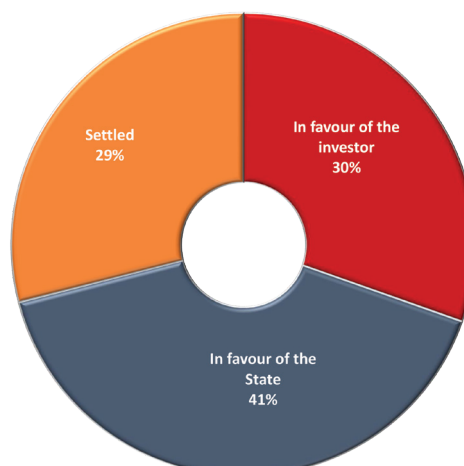


Figure 3: Concluded ISDS Proceeding Outcomes



Source: UNCTAD ISDS Database, accounting for 608 ISDS claims from 1987 to 2014, of which 362 cases were concluded either in favour of the state or investor, or via settlement among disputing parties; Author's calculations.²¹

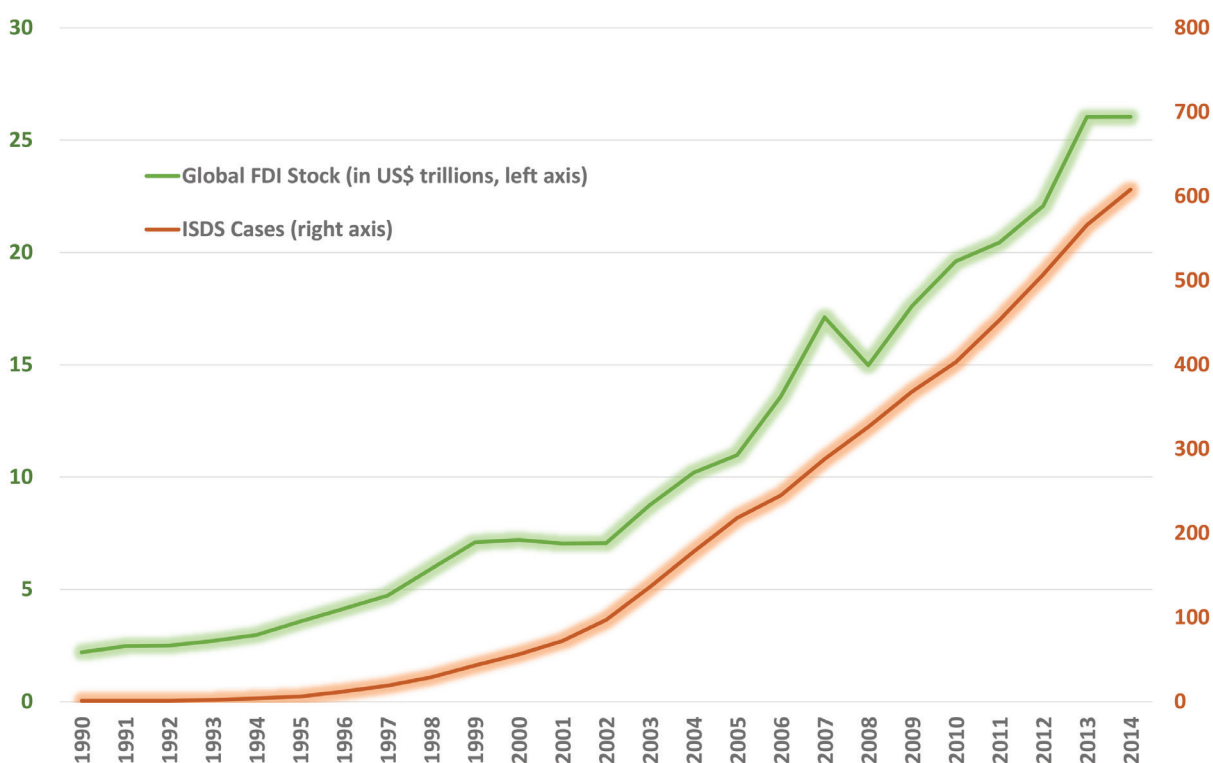


The Global Rise of ISDS Cases

The number of ISDS cases filed for arbitration between a private investor and a sovereign state has accelerated since the turn of the millennium as globalised capital flows and new international investment agreements proliferate.²² The end of the Cold War and advancements in information technology birthed numerous possibilities for foreign investment in new markets throughout the globe²³ — and with the increase in foreign direct investment, international disputes between foreign

investors and host governments started to increase (**Figure 4**). According to the United Nations Conference on Trade and Development (UNCTAD), there were just under 100 ISDS cases initiated between 1987 (the beginning of the data series) and 2002; but with an average of 43 new cases per year since 2003, the total amount of known ISDS cases is currently at 608 initiated disputes.²⁴

Figure 4: Globalisation and ISDS Cases



Source: UNCTAD; Author's calculations.²⁵

The Development Status of Disputing Parties

Figure 5 depicts the annual rise of known ISDS cases filed since 1987, indicating the development status of both investor claimants and state respondents. Roughly half of all ISDS cases relate to investors from developed home states bringing non-developed states to arbitration. Nonetheless, more and more developed states are figuring among respondents of ISDS cases, largely as a result of claims by other developed home state investors comprising a quarter of all cases.

The composition of parties involved in ISDS cases has started to shift in recent years, mimicking the rise of emerging markets as both capital importers and exporters. Since 2003, the number of investor claimants from non-developed home states have been on a firm rise — with its share growing from 7% of ISDS cases until 2002 to 27% during the last five years.²⁶

Despite more than 100 nations being involved in ISDS proceedings, there is still a sizable concentration among a few countries when analysing the nationality of investor claimants and state respondents (**Table 1**). As expected, countries with a long history of high FDI outflows are more likely to have their national investors under arbitral disputes against foreign governments. The United States leads the home state investors ranking with 134 ISDS cases, or 22% of the total; followed by the Netherlands (70 ISDS cases), United Kingdom (49) and Germany (42).²⁸ These four countries alone account for half of all home state claimants in ISDS cases.

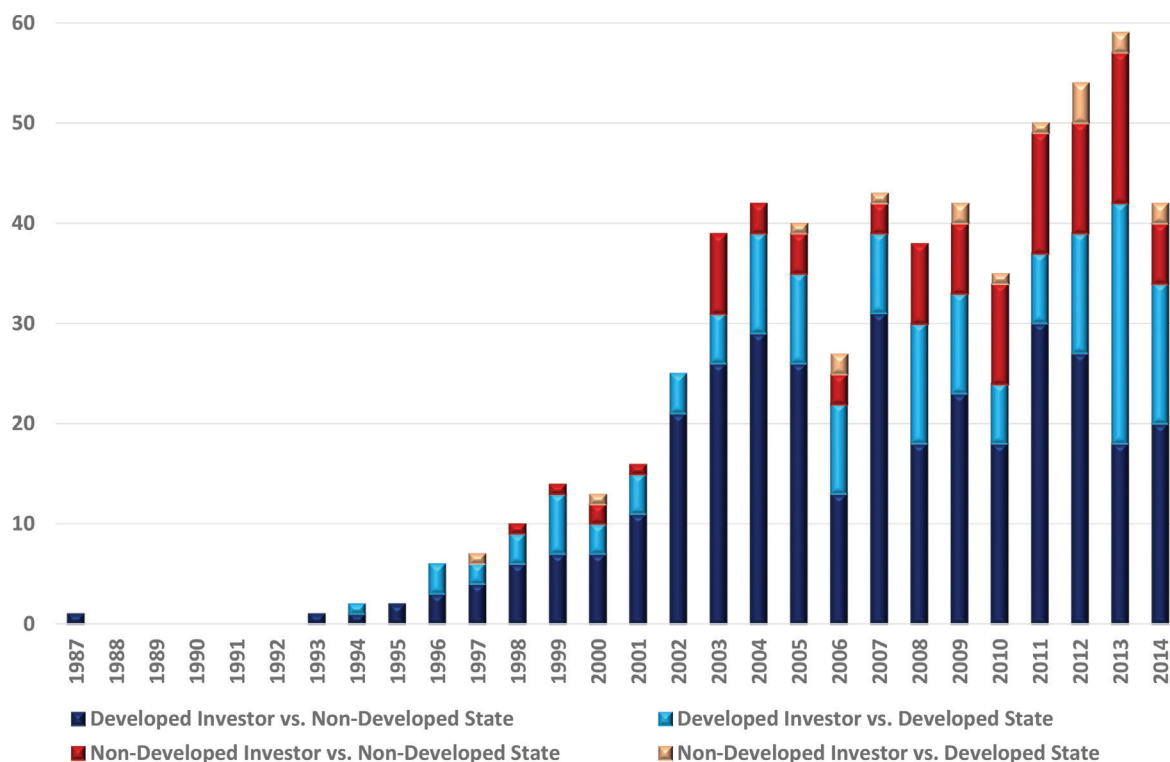
Table 1: Most Frequent Respondents and Claimants in ISDS Cases (number of cases within brackets)

	State Respondents	Home State Claimants
1	Argentina (56)	United States (134)
2	Venezuela (36)	Netherlands (70)
3	Czech Republic (29)	United Kingdom (49)
4	Egypt (24)	Germany (42)
5	Canada (23)	Canada (35)
6	Ecuador (21)	France (35)
7	Mexico (21)	Spain (28)
8	India (16)	Italy (27)
9	Ukraine (16)	Switzerland (19)
10	Poland (15)	Luxemburg (19)
11	United States (15)	Turkey (18)
12	Kazakhstan (14)	Belgium (14)
13	Spain (14)	Austria (13)
14	Hungary (13)	Cyprus (13)
15	Slovakia (12)	Russia (12)

Source: UNCTAD; Author's calculations.²⁹

NB. Cases started by investors from more than one country are counted for each country.

Figure 5: Annual Rise of ISDS Arbitral Proceeding Claims



Source: UNCTAD; Author's calculations.²⁷

NB. Development status according to the UN *World Economic Situation and Prospects* (2016) classification. Investor's classification is based on the respective home state's development status.

Although most top 15 investor claimants are originally from high-income developed countries, the growing presence of emerging economies is notable. In particular, ISDS claimants from Turkey (18 cases), Russia (12), Chile (6) and China (4) have been rising.³⁰

When it comes to state respondents, national governments under a weak rule of law environment tend to prominently feature in ISDS cases. Indeed, Abbott *et al.* (2014) shows that countries with low-quality legal frameworks are more likely to figure as state respondents in ISDS disputes.³¹ As representative cases, Argentina and Venezuela are by far the most targeted countries, having responded to 56 and 36 ISDS cases, respectively. After more than a decade of rogue and populist national leaderships, these two Latin American countries have become the public face of ISDS respondents.

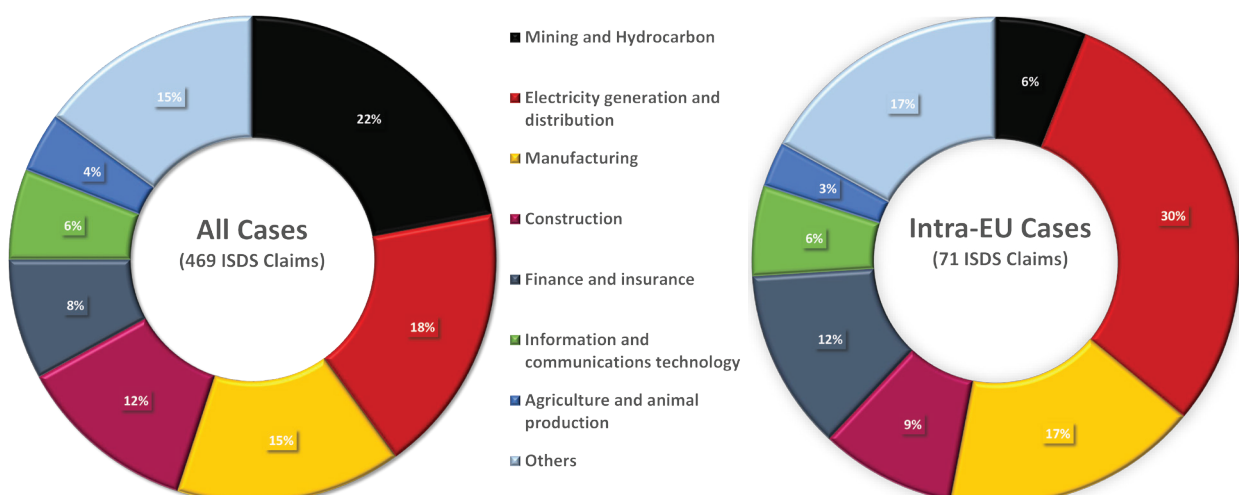
However, as noted above, developed nations are increasingly facing ISDS claims. Most notably, Canada (23 ISDS cases), United States (15) and Spain (14) appear in the top 15 most frequent respondents.³² Despite these countries' sound legal system and strong rule of law culture, a sizeable incoming FDI stock and a copious number of international investment agreements are proof no nation is immune to legitimate investor-state disputes. And indeed, nor are they immune to international investment breaches by national governments: although the US government has never lost an ISDS case, it has settled in three proceedings;³³ Canada has had three adverse rulings and has settled in four other cases;³⁴ and Spain has lost one proceeding, with all other ISDS cases still awaiting a final ruling.³⁵

A Sectorial Analysis of ISDS Cases

When measuring ISDS cases by sector, evidence shows that industries characterised by high levels of state intervention — and therefore more prone to government misconduct — have a greater representation in arbitral disputes. In a study conducted by the European Centre for International Political Economy,³⁶ researchers found that the *mining and hydrocarbon* industries are the leading sector in the 469 ISDS claims filed between 2003 and 2013, comprising 22% of disputes; followed by *electricity generation and distribution*, which accounted for 18% of the total (**Figure 6**). Both sectors feature conspicuous state involvement, either through heavy regulation and/or joint-ventures with state companies. Other sectors with relevant representation in ISDS disputes — and at times also facing strong state intervention — are *manufacturing* (15% of the ISDS claims in the study period), *construction* (12%), and *finance and insurance* (8%).

The same study also analysed the subset of intra-EU ISDS cases — claims where both investor claimant and state respondent are from the European Union. In total, there were 71 intra-EU ISDS disputes between 2003 and 2013. This subsample is a good proxy for determining whether disputes involving only developed home and respondent states deviate from the overall ISDS sectorial pattern. Results indicate that apart from a reduced proportion of disputes involving the *mining and hydrocarbon* sector (just 6% of all ISDS claims) — in this case mostly due to the small size of the sector in the EU — the sectorial distribution of ISDS disputes is not much different from the overall population of ISDS cases. *Electricity generation and distribution* still features a prominent involvement in intra-EU cases, accounting for 30% of the sample; followed by *manufacturing* (17%), *finance and insurance* (12%) and *construction* (9%). That is, regardless of the development status of the investor's home state and host governments, evidence confirms that ISDS cases tend to consist of sectors with high state involvement.

Figure 6: ISDS Cases by Sector (2003–2013)



Source: European Centre for International Political Economy³⁷

ISDS Winning Odds

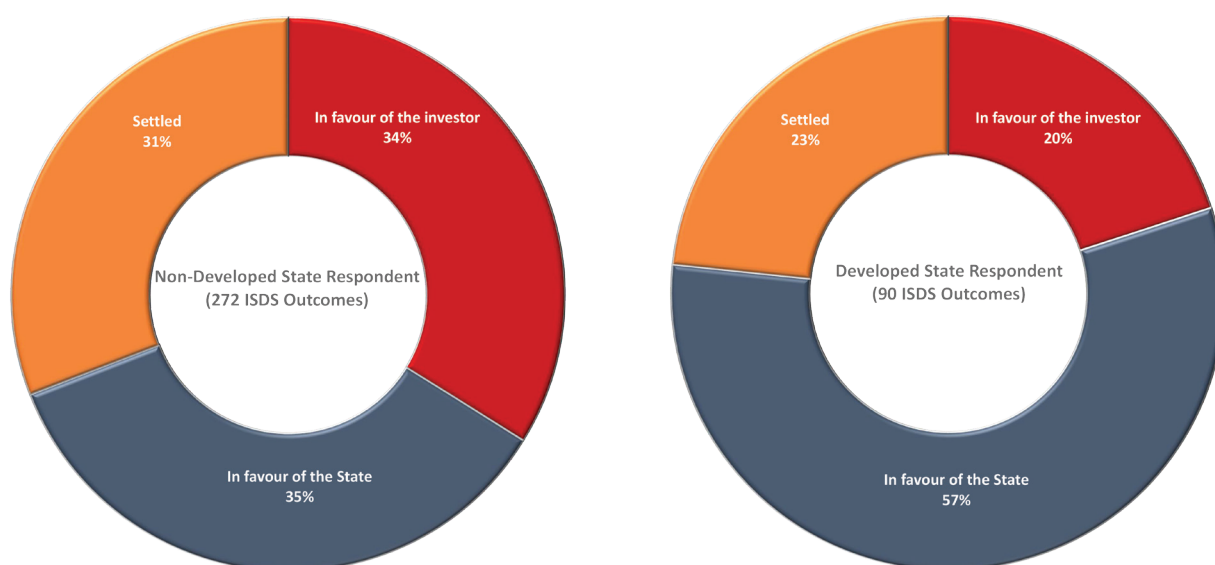
According to the UNCTAD database, there are 362 known concluded ISDS arbitration cases in the past 30 years that were either ruled in favour of the investor (110 cases) or the state (147 cases), or a settlement was reached between disputing parties under the auspices of the ISDS tribunal (105 cases).³⁸ These concluded cases show a balanced historical score for both claimants and respondents, and a great deal of consensus building among disputing parties through homologated settlements.

However, results are somewhat different when taking into account the rule of law environment where foreign investments were made. In **Figure 7**, ISDS arbitration outcomes are displayed according to the development status of state respondents, which could be interpreted as a proxy for the degree of law-abiding governments and a reliable domestic justice system (that assist as a further restraint against unlawful government acts).

In summary, ISDS rulings when the respondent is a developed state are much less likely to be proved guilty: of 90 concluded ISDS cases, 57% were in favour of the developed state, 20% in favour of the investor, and the remaining 23% were settled between the disputing parties.³⁹ In the developed world, the biggest losers in ISDS proceedings are Canada and Czech Republic, with three adverse rulings each.⁴⁰

When ISDS cases against non-developed state respondents are measured, investor claimants are as likely to win the case as state respondents. Of a total of 272 concluded cases, 35% were in favour of the non-developed state, 34% in favour of the investor, and 31% settled via mutual agreement.⁴¹ As the worst offender of international investment agreements, Argentina has already lost 13 ISDS proceedings, followed by Mexico (9 unfavourable rulings), Kyrgyzstan (6), Venezuela (6) and Russia (6).⁴²

Figure 7: ISDS Arbitration Outcome by development status of state respondents



Source: UNCTAD; Author's calculations.⁴³

NB. ISDS arbitration outcomes do not account for discontinued cases or treaty breaches with no monetary compensation awarded.



ISDS in Australia's Politics and International Agreements

The history of investor-state arbitration in Australia's politics and international agreements has been a swinging pendulum between complete embrace and outright rejection. Currently, Australia's official policy on the ISDS provisions runs on a case-by-case basis, zig-zagging between the need to spur the rule of law in the international arena and fears about the impact of ISDS rulings on national sovereignty. In total, Australia has ISDS provisions in 21 bilateral investment treaties and seven free trade agreements (**Table 2**).

The Hawke and Keating Governments

The Hawke and Keating governments seized the opportunity to embrace investor-state arbitration, recognising the benefits of expanding the rule of law globally and of being an active player in the process. The first ISDS-protected agreement was signed with China in 1988,⁴⁴ marking the beginning of a golden era for investor-state arbitration support both here and overseas. Under Hawke and Keating, Australia signed further bilateral investment treaties with Papua New Guinea (1990), Vietnam (1991), Poland (1991), Hungary (1991), Indonesia (1992), Romania (1993), Hong Kong (1993), Czech Republic (1993), Laos (1994), Philippines (1995), Argentina (1995), and Peru (1995).⁴⁵

In line with the international practice of the time, the first wave of Australia's ISDS-protected international agreements for 'the reciprocal promotion and protection of investments'— as these agreements were named⁴⁶ — was marked by the use of very vague language, with few qualifications and a lack of precise definition on key terms. Much of the agreements' crude wording was due to a still fledgling BIT global environment, with only a handful of ISDS disputes to guide international treaty's lawmaking.

With roughly 15 standardised articles, all these Australian BITs display very similar phrasing — if not the same in most cases — essentially prescribing: "*Each party shall ensure fair and equitable treatment in its own territory to [the respective foreign national's] investments and associated activities*"; "*...no less favourable than accorded to investments and associated activities of investors of any other third country [i.e. Most Favoured Nation provision]*"; and "*Neither Contracting Party shall nationalise, expropriate or subject to measures having effect equivalent to nationalisation or expropriation the investments of investors of the other Contracting Party unless the following conditions are complied with: (a) the expropriation is for a public purpose related to the internal needs of that Contracting Party and under due process of law; (b) the expropriation is non-discriminatory; and (c) the expropriation is accompanied by the payment of prompt, adequate and effective compensation*".⁴⁷ Most importantly, all these BITs provide the option for the settlement of international disputes in investor-state arbitration tribunals, commonly with the World Bank's International Centre for the Settlement of Investment Disputes (ICSID) being the first arbitral forum of choice.

Table 2: Australia's ISDS-Protected Agreements

Bilateral Investment Treaties		
Signed In	Entry into Force	BIT with
1988 (July)	1988 (July)	China
1990 (September)	1991 (October)	Papua New Guinea
1991 (March)	1991 (September)	Vietnam
1991 (May)	1992 (March)	Poland
1991 (August)	1992 (May)	Hungary
1992 (November)	1993 (July)	Indonesia
1993 (June)	1994 (April)	Romania
1993 (September)	1993 (October)	Hong Kong
1993 (September)	1994 (June)	Czech Republic
1994 (April)	1995 (April)	Laos
1995 (January)	1995 (December)	Philippines
1995 (August)	1997 (January)	Argentina
1995 (December)	1997 (February)	Peru
1998 (February)	1998 (October)	Pakistan
1998 (November)	2002 (May)	Lithuania
1999 (February)	2000 (May)	India
2001 (May)	2002 (September)	Egypt
2001 (September)	2002 (December)	Uruguay
2002 (November)	2007 (March)	Sri Lanka
2005 (June)	2009 (June)	Turkey
2005 (August)	2007 (July)	Mexico

Free Trade Agreements		
Signed In	Entry into Force	FTA with
2003 (February)	2003 (July)	Singapore
2004 (July)	2005 (January)	Thailand
2008 (July)	2009 (March)	Chile
2014 (April)	2014 (December)	Korea
2014 (August)	2015 (October)	ASEAN and New Zealand
2015 (July)	2015 (December)	China
2016 (February)	---	Trans-Pacific Partnership

Source: Australia's Department of Foreign Affairs⁴⁸

NB. ASEAN members are Indonesia, Malaysia, Philippines, Singapore, Thailand, Brunei, Vietnam, Laos, Myanmar and Cambodia; TPP members are Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, Peru, New Zealand, Singapore, the United States and Vietnam.

The Howard Government

The change of government in early 1996 did not result in a rupture of Australia's previous BIT model — including the same vague wording and format of investment-protected agreements — with continued promotion of Australia's new bilateral treaties. Under Howard's tenure, the Australian government signed further bilateral agreements with Pakistan (1988), Lithuania (1998), India (1999), Egypt (2001), Uruguay (2001), Sri Lanka (2002), Turkey (2005), and Mexico (2005).⁴⁹

However, as global multilateral trade talks began to show faltering signs in the 2000s — of which the still lingering Doha Development Round is a prime example — the attractiveness of more extensive and viable regional and bilateral trade agreements became clear. Under this refreshed trade talk environment, a new breed of broader and more detailed-oriented ISDS agreements began to emerge in Australia's foreign affairs.

During the Howard administration, Australia signed free trade agreements with Singapore (2003) and Thailand (2004) containing ISDS-protected investment chapters with new features that better qualified the right of foreign investors to seek reparation in international arbitral tribunals. For instance, by explicitly exempting government grants, subsidies and procurement matters from investor-state arbitral disputes, Australia formally recognised limits to the national treatment given to foreign investors.

In particular, the Singapore-Australia Free Trade Agreement (SAFTA) went even further, specifying the legitimate use of ISDS provisions. For example, for the first time in Australia's investment agreements, foreign investors would face a statute of limitation (i.e. investors would have a three-year maximum period after a treaty obligation breach to seek reparation in arbitral proceedings).⁵⁰ In addition, concepts such as 'fair and equitable treatment' and 'full protection and security' were properly narrowed under the customary international law minimum standard of treatment:

"Article 4: Minimum Standard of Treatment

1. *Each Party shall accord to investments of investors of the other Party treatment in accordance with the customary international law minimum standard of treatment of aliens, including fair and equitable treatment and full protection and security.*

2. *For greater certainty, the concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens referred to in paragraph 1 and do not create additional substantive rights. The obligation in paragraph 1 to provide:*

(a) "fair and equitable treatment" includes the obligation not to deny justice in

criminal, civil or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world; and

*(b) "full protection and security" requires each Party to provide the level of police protection required under customary international law."*⁵¹

Furthermore, SAFTA features important exemptions to ISDS protection, such as: restrictions to safeguard the country's balance of payments (*"In the event of serious balance of payments and external financial difficulties or threat thereof, a Party may adopt or maintain restrictions on payments or transfers related to investments"*);⁵² exceptions for legitimate national security reasons and public order, and for other general purposes such as protecting *"human, animal or plant life or health"*.⁵³

It seemed SAFTA — and to a certain extent the Australia-Thailand FTA — represented a renewed and enlightened commitment from Canberra to adopt and modernise the use of investor-state arbitration in Australia's investment agreements. Nonetheless, a last-minute political decision to drop ISDS provisions from the Australia-United States Free Trade Agreement (AUSFTA) in 2004 represented the first major setback in Australia's ISDS history.⁵⁴ The Australian government line was that *"Reflecting the fact that both countries have robust, developed legal systems for resolving disputes between foreign investors and government, the Agreement does not include any provisions for investor-state dispute settlement"*.⁵⁵ Yet, the truth appears to be otherwise.

For a start, the assumption that ISDS provisions should not be part of international agreements between developed nations is still open to debate.⁵⁶ Moreover, even if the Howard government's statement regarding the lack of necessity for ISDS provisions between developed nations were genuine, it still begs the question of why the same provisions were fully endorsed a year before in the Australia's free trade agreement with Singapore — a high-income nation with a respectable record on the rule of law that ranks in the top positions of the Economic Freedom Index (ahead of Australia and the US),⁵⁷ as well as sits in the highest ranks of the World Economic Forum's Index on Efficiency of legal framework in Challenging Regulations and Settling Disputes.⁵⁸

In reality, the truth resides in Australia's domestic politics itself: the Howard government decided to withdraw the ISDS provisions from AUSFTA fearing the agreement would not be ratified in parliament. As Tienhaara and Ranald (2011) point out, the Australian Labor Party (ALP), the Greens and the Democrats all strongly opposed ISDS provisions in the agreement and *"because these parties held a majority of Senate seats, they had the option of blocking the implementing legislation for the AUSFTA"*.⁵⁹

The Rudd-Gillard-Rudd ALP Government

The rise of the ALP to federal government at the end of 2007 truly depicts the swinging pendulum of the ISDS debate in national politics, moving from initial support to outright rejection. The 2008 Australia-Chile Free Trade Agreement signed during Kevin Rudd's first term represents the most advanced ISDS-protected agreement in Australia's history up to that point. Not only did the document maintain the improvements present in SAFTA, but it also included a list of new features in accordance with the most recent state-of-the-art investment agreements worldwide, such as:

- *Amicus Curiae*: the ability of interested parties (e.g. NGOs, informed citizens, investor's home state government) to provide written submissions to the arbitral tribunal;⁶⁰
- *Full transparency of arbitral proceedings*: endorsing the global push to end the secrecy of ISDS proceedings, without compromising sensitive confidential information from the disputing parties;⁶¹
- *Consolidation of ISDS claims*: the ability to amalgamate two or more ISDS claims that share in common a question of law or fact and arise out of the same events or circumstances;⁶²
- *No U-turn clause*: in order to submit an ISDS claim, the claimant must waive its right to initiate or continue parallel claims in any other forum, including domestic courts;⁶³
- *Summary decision on frivolous claims*: the arbitral tribunal shall decide to end the dispute "on an expedite basis" when there is a valid objection to the forum's competence or jurisdiction;⁶⁴
- *Financial compensation nature of awards*: express mention that the arbitral tribunal may only award non-punitive, monetary damages and/or restitution of property, i.e. no jurisdiction over sovereign legislation *per se*;⁶⁵
- *Interim review of awards*: the ability of the disputing parties to request revision or annulment of the award before it is made final;⁶⁶
- *Qualification of indirect expropriation*: demanding indirect expropriations to be treated case-by-case, and "except in rare circumstances, non-discriminatory regulatory actions by a [Sovereign] Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations";⁶⁷
- *Expert Reports*: ability for the disputing parties to appoint "one or more experts to report to it in writing on any factual issue concerning environmental, health, safety or other scientific matters";⁶⁸
- *Legal Cost Recovery*: the possibility for winner disputing party to recover costs on the legal proceedings and attorney's fees.⁶⁹

In short, the ISDS provisions in the Australia-Chile Free Trade Agreement were a step in the right direction. Yet

the rising momentum was short-lived: no other ISDS-protected agreement was signed by Australia until the end of the Rudd-Gillard-Rudd Labor Government. And worse, during the second half of Labor administration, the Australian official policy on ISDS provisions in future agreements became one of outright rejection — and made Australia the first and only developed country to do so.⁷⁰

On April 12th, 2011, the Australian Government released a Trade Policy Statement condemning the purpose of investor-state arbitration:

"The Gillard Government...does not support provisions that would confer greater legal rights on foreign businesses than those available to domestic businesses. Nor will the Government support provisions that would constrain the ability of Australian governments to make laws on social, environmental and economic matters in circumstances where those laws do not discriminate between domestic and foreign businesses. The Government has not and will not accept provisions that limit its capacity to put health warnings or plain packaging requirements on tobacco products or its ability to continue the Pharmaceutical Benefits Scheme. In the past, Australian Governments have sought the inclusion of investor-state dispute resolution procedures in trade agreements with developing countries at the behest of Australian businesses. The Gillard Government will discontinue this practice. If Australian businesses are concerned about sovereign risk in Australian trading partner countries, they will need to make their own assessments about whether they want to commit to investing in those countries."⁷¹

The Statement was largely based on disputed assumptions concerning investor-state arbitration: that ISDS constrains the sovereign ability to legislate (see *Myth 2 in Debunking the Seven ISDS Myths*); that ISDS confers greater legal rights to foreigners (*Myth 3*); that ISDS should be included in trade agreements only with developing countries (*Myth 4*); that ISDS is a redundant tool to overcome political risks (*Myth 5*).

Nonetheless, there were a few further reasons behind this abrupt change of heart towards investor-state arbitration for the newly elected Gillard Government. First, there was the concern that the Australian Greens — the government's key supporting partner in power — would effectively once again be able to block any trade deal containing ISDS provisions.⁷²

Second, in a report published a year before the 2011 Trade Statement, the Productivity Commission had downplayed the role of ISDS provisions.⁷³ Despite some relevant criticisms against the PC recommendations on investor-state arbitration — as outlined by the Director of the International Investment Law Research Programme at the University of Melbourne, Prof Jürgen

Kurtz, “the [Productivity] Commission’s framing and analysis of investment disciplines [in the Research Report on Bilateral and Regional Trade Agreements] is shallower and less sophisticated, perhaps reflecting its inexperience with international law”⁷⁴ — the document provided further intellectual ammunition to the ALP government decision to issue the ISDS-condemning policy.⁷⁵

Third, there was great uproar regarding the looming ISDS case on Australia’s tobacco plain packaging legislation that was brought under UNCITRAL rules at the end of 2011 — the first and only ISDS claim against

Australia, which was later dismissed by the arbitral tribunal (see *Appendix: The ISDS Cases involving Australian Investors and Government*).⁷⁶

Notwithstanding the strong ISDS condemnation proclaimed in the 2011 Trade Statement, Australia’s rejection of investor-state arbitration clauses was short-lived, with only the ISDS-free Australia-Malaysia Free Trade Agreement signed in 2012 affected by it. Indeed, under the new Coalition government elected in September 2013, ISDS negotiations were back on the table — albeit under a ‘case-by-case basis’.⁷⁷

The Current Coalition Government

Under the leadership of Federal Minister for Trade and Investment Andrew Robb, Australia successfully fast-tracked the conclusion of five free trade agreement negotiations — with Japan (2014), Korea (2014), ASEAN countries and New Zealand (2014), China (2015) and the Trans-Pacific Partnership members (2016).⁷⁸ Indeed, through varying routes, Australia formalised ISDS provisions with all the countries involved, including amending the lack of investor-state arbitration clauses in the agreements previously signed with Malaysia (through the ASEAN-NZ-Australia FTA) and the United States (through the TPP).

Further, although the Japan-Australia FTA excluded ISDS arrangements, the same investor protection was included in the TPP agreement, of which both countries are signatories. The same logic was also applied to previous commitments between Australia and New Zealand in 2009 to opt out of ISDS provisions contained in the ASEAN-NZ-Australia FTA;⁷⁹ both countries now have ISDS-protected investments with each other through the recently concluded TPP agreement.

Most importantly, the free trade agreements signed with Korea (2014), ASEAN (2014), China (2015)⁸⁰ and the TPP (2016) all included an improved set of ISDS provisions, such as allowing for signatory countries to issue binding interpretations on ISDS clauses, further limitations of ISDS scope on sensitive regulatory areas, and plans to build an effective appellate review mechanism.⁸¹

In summary, ISDS provisions in Australia’s history have come a long way, from simple and rudimentary clauses found in the first wave of BITs to the latest protections in recent free trade agreements; from total political acceptance to outright rejection to current hesitant case-by-case basis. It is time to renew our national commitment to this important international legal institution. Hopefully, as ISDS cases increasingly become part of the international legal framework — including with Australian investors and the Australian government as disputing parties — the myths about investor-state arbitration will be debunked while the benefits from a stronger international rule of law become more evident.



The Case for Investor-State Arbitration

There are many benefits from introducing ISDS provisions in international agreements. First and foremost, the case for investor-state arbitration lies in the strengthening of the rule of law — the quintessential feature of free markets and individual liberty, and indeed a cornerstone to human prosperity since Magna Carta.⁸² In Hayek's words:

*"Stripped of technicalities this [the Rule of Law] means that government in all its actions is bound by rules fixed and announced beforehand – rules that make it possible to foresee with fair certainty how the authority will use its coercive powers in given circumstances and to plan one's individual affairs on the basis of this knowledge. Thus, within the known rules of the game, the individual is free to pursue his personal ends, certain that the powers of government will not be used deliberately to frustrate his efforts."*⁸³

And that is precisely what investor-state arbitration achieves in the international arena: legal predictability and equality among disputing parties who do not necessarily share the same domestic legal values and customs.

In addition, despite being an international remedy for a breach of international obligations, ISDS has important beneficial spill-over effects on the rule of law for the host's citizens, who tend to be increasingly vocal in their demand for a law-based democratic system. As international legal expert John Veroneau puts it, *"it is more likely that extending protections to foreign property owners would instil demand for more protections for domestic property owners. Calls for domestic property protections would seem to get louder if such protections are extended to foreign property owners"*.⁸⁴

Another important ISDS corollary regards the introduction of competition in the delivery of justice — and again benefiting not just foreign investors but also domestic citizens. Most ISDS provisions allow international investors to choose whether to pursue their grievances in either domestic courts or *ad hoc* tribunals. Given that third-party arbitration is fundamentally based on impartial adjudication — and therefore does not intrinsically increase the chance of a successful claim⁸⁵ — both national and international jurisdictions are set to compete on other fronts: umpire expertise, costs, expediency, flexibility, and so forth. Such a race for excellence ends up breaking one of the last frontiers of national monopoly, the domestic judicial system, resulting in an enhanced rule of law administration for all users.

Further, ISDS is a non-belligerent alternative to state-to-state dispute escalation, reducing the necessity of international sanctions or even 'gunboat diplomacy', where powerful states would threaten to (or actually) militarily intervene in other sovereign nations in order to secure private commercial interests.⁸⁶ In effect, by subrogating to private citizens the right to correct treaty breaches, investor-state arbitration provides a depoliticised hearing without tarnishing the relationship between sovereign nations; and at the same time, saves the need for investors to convince a home state government to espouse their claims at the risk of jeopardising higher national goals.⁸⁷

Also important is the ISDS ability to reduce the sovereign risks associated with investments across borders, by providing an effective remedy to curb unlawful treatment from host governments. Hence, despite many other factors playing on FDI decisions, and the difficulty of quantifying the impact of ISDS on cross-border investments, a safer environment for international investments invariably ends up benefiting both importers and exporters of capital.⁸⁸

Recommendation: Australia should fully embrace investor-state arbitration

Australia has much to gain by fostering the rule of law in international affairs through the welcoming of investor-state arbitration provisions in international agreements. In the past 30 years since Australia's first ISDS-protected treaty, the world has become a safer place for Australian investors, with investor-state arbitration acting as a powerful and effective Sword of Damocles against unlawful foreign government acts — and in three occasions indeed providing a neutral and de-politicised forum to assert a just treatment of Australian interests overseas.

Domestically, ISDS provides an extra check on our judicial and political systems to ensure they remain fair and expedient in the treatment of very welcome international investments. Further, ISDS brings little disruption to our domestic affairs, given the high standards of Australia's rule of law culture; the first and only ISDS case against the Australian government (on tobacco packaging legislation) has been recently dismissed.

In short, the system works. And that's the beauty of the rule of law: those who owe nothing have nothing to fear.

Addressing Valid Concerns

This is not to say that ISDS arrangements are perfect. Like any other system, there is always room for corrections, and investor-state arbitration is no different. In particular, three areas need improvement.

1. Transparency of ISDS proceedings

The current transparency deficit in ISDS proceedings constitutes a major hurdle to attracting community support, inflating fears and myths around investor-state arbitration. As outlined by the UNCTAD, *"One of the key issues in ISDS is the question of transparency. Providing increased and better access to information about ongoing disputes and about the ISDS process generally is one of the primary tools available to respond to concerns about the legitimacy of ISDS."*⁸⁹ Indeed, public scrutiny over ISDS rulings is critical to boost their democratic credentials.

In recognising the void, much has been done to bring ISDS cases into the daylight in the last decade — yet the process is still far from complete. Accordingly, the two main arbitration forums have already started to reform themselves in order to increase transparency in investor-state disputes.⁹⁰ For instance, the World Bank's International Centre for Settlement of Investment Disputes (ICSID) has boosted its transparency rules since 2006, including authorising the publication of

excerpts of the tribunal's legal reasoning.⁹¹ In addition, all disputes are now listed on a public registry. However, notwithstanding these improvements, award confidentiality is still an option for the disputing parties.⁹²

The United Nations Commission on International Trade Law (UNCITRAL) has also started — albeit at a slower pace than ICSID — to introduce greater transparency into its ISDS proceedings.⁹³ Yet it is important to understand that the United Nations' arbitration facility is more akin to its roots in international commercial arbitration, where confidentiality of proceedings has been the hallmark since its origin. Currently, the very existence of ISDS cases can remain hidden from the public if both disputing parties so decide. Nonetheless, following a major overhaul initiated in 2010, a new set of transparency rules has been implemented; although it is worth noting that such measures still have to be agreed in future IIAs or by the disputing parties before coming into force.⁹⁴

Recommendation: Transparency of ISDS procedures should be the rule

Australia should keep its commitment to international efforts on fostering transparency in the investor-state dispute arena. Indeed, all of Australia's ISDS-protected agreements since 2008 have formal clauses on 'Transparency of Arbitral Proceedings', demanding hearings and related documents to be open to the public after protecting any legitimate sensitive information. However, Australia can still play a more active part by pre-emptively consenting to open hearings and the lawful disclosure of related documents at all times, including for disputes based on previous ISDS agreements where transparency of proceedings is not the rule.

2. A well-delimited and legitimate use of ISDS

ISDS critics often rush to cite rogue cases where investor claimants exploit poor wording provisions in international treaties to game the system: e.g. excessive delays to initiate a claim; improper interpretation of treaty provisions; forum and treaty shopping; disproportionate financial compensation awards; inadequate indirect expropriation qualification; and most-favoured-nation clause abuses.⁹⁵

Fortunately, valid concerns about misuses by ISDS claimants have been channelled to perfect the system instead of becoming an outright rejection of investor-state arbitration.⁹⁶ For instance, most recent international agreements (including the Trans-Pacific Partnership) now provide important checks and balances in the access to investor-state arbitration, such as:⁹⁷

- Defined statute of limitation and cool-off periods on initiating a claim;
- Public participation option via *amicus curiae* submissions;
- Mechanism for treaty parties to issue binding decisions on how to interpret treaty provisions;
- Award restrictions to non-punitive monetary compensation;
- Proper guidelines on indirect expropriation assessments;

- Strict limits to investment protection coverage on sensitive regulatory areas;
- Expedited review and dismissal of frivolous claims;
- Interim review of awards before rulings are made final;
- Restrictions on parallel claims, including blocking the access to domestic courts once an ISDS case is initiated (No U-Turn policy);
- Clear rules on challenging an ISDS award.

Indeed, after almost 60 years since the first ISDS-protected international agreement and more than 600 known cases, the design of investor-state arbitration provisions have been in constant evolution — including amid Australia’s international investment treaties.⁹⁸ It is important to understand, however, that the process of fine tuning ISDS provisions needs to be a constant and vigilant effort not to undermine the core purpose of investor-state arbitration. As warned by UNCTAD, “*It should be noted that qualifying and/or introducing limitations to ISDS provisions... can contribute to reducing the protective coverage of the treaty in question, and thereby, undermine its quality as an investment tool.*”⁹⁹

Recommendation: ISDS provisions should ensure a well-delimited and legitimate use of investor-state arbitration

Australia should maintain its international efforts to ensure ISDS-protected agreements are fit for purpose by ensuring a well-delimited and legitimate use of investor-state arbitration. The real challenge is to get the Goldilocks balance between proper limitations and valid coverage — for which the recent TPP state-of-the-art investment chapter constitutes a good yardstick.

3. Consistency of ISDS rulings and provisions

An area ripe for improvement is the consistency of ISDS rulings and provisions. Whereas divergent jurisprudence for similar cases undermines the predictability of ISDS protection; discrepancy in ISDS provisions among different international agreements can open room for *treaty shopping*, where “*an investor structures an investment (through incorporation and possibly by restructuring certain business operations) in order to seek to qualify for protections conferred by particular investment treaties*”.¹⁰⁰

Some of the remedies to avoid the threat of treaty shopping are to prohibit the use of shell companies accessing ISDS (as done in the TPP) and to restrict the use of most-favoured-nation clauses.¹⁰¹ However,

ideally the problem would be more effectively dealt with by aligning ISDS provisions in international agreements — which is easier said than done, as that path would involve extensive diplomatic renegotiations with several trade partners.

With respect to the consistency of rulings, including the possibility of repealing defective awards, there is an intense international debate about promoting appellate mechanisms.¹⁰² The challenge is to allow a second-level appeal body without excessively penalising the expediency and legal costs of ISDS proceedings.

Indeed, some recent ISDS-protected agreements already allow the creation of appellate mechanisms, although

leaving implementation details for further regulation. For instance, Australia's Free Trade Agreements with Korea and China stipulate *"within three years after the date of entry into force of this Agreement, the Parties shall consider whether to establish a bilateral appellate body or similar mechanism to review awards"*.¹⁰³

Similar provisions are also included in the TPP:

"In the event that an appellate mechanism for reviewing awards rendered by investor-State dispute settlement tribunals is

developed in the future under other institutional arrangements, the Parties shall consider whether awards rendered under Article 9.29 (Awards) should be subject to that appellate mechanism. The Parties shall strive to ensure that any such appellate mechanism they consider adopting provides for transparency of proceedings similar to the transparency provisions established in Article 9.24 (Transparency of Arbitral Proceedings)."¹⁰⁴

Recommendation: An ISDS appellate mechanism should be implemented

Australia should maintain its international efforts to implement an ISDS appellate mechanism. Such second-instance adjudication forum, however, should not excessively penalise the expediency and legal costs of investor-state arbitration disputes.

Recommendation: Whenever possible, previous ISDS commitments should be realigned to the latest advancements in investor-state arbitration provisions

Since 1988, Australia has agreed to ISDS provisions in 21 bilateral investment treaties and seven free trade agreements. As this report outlines, there has been a steep evolution in investor-state arbitration clauses, with stark differences between Australia's first investment-protected agreements compared to more recent ones (in particular to the TPP state-of-the-art investment chapter). Therefore, Australia must work with its trading partners to ensure that previous ISDS commitments are updated and consistent with a transparent, well-delimited and legitimate use of investor-state arbitration.



Debunking the Seven ISDS Myths

Myth 1: ISDS breaches sovereign immunity

Truth: ISDS is a conscious act of sovereignty

ISDS detractors are quick to criticise the legitimacy of investor-state arbitration, questioning the adjudication powers of a collegiate of appointed umpires outside domestic courts.¹⁰⁵ As claimed by a European Greens member, *"Using this [ISDS] mechanism, foreign investors can circumvent national courts and sue a state before an international arbitration court if they believe their rights have been violated ... Democratic decision-making is forcefully going under the knife through international arbitration."*¹⁰⁶ Under the same indictment, others have criticised the ISDS system as "flawed",¹⁰⁷ "unfair, unsustainable, and under the radar",¹⁰⁸ and a "privileged corporate justice system".¹⁰⁹

The same critical voices are also heard in Australia: for instance, the Australia Services Union condemns ISDS provisions for *"undermin[ing] democratic processes by enabling foreign investors to sue governments for compensation"*;¹¹⁰ the Australian Fair Trade and Investment Network, a network of 60 community organisations, rejects investor-state arbitrations as an *"unacceptable expansion of the rights of corporate investors at the expense of democratic government"*;¹¹¹ Chief Justice RS French AC questioned the democratic credentials of ISDS challenges to decisions of a domestic

court;¹¹² the Australian Greens call it a *"Trojan Horse in our secretive trade agreements"*.¹¹³

That is, critics claim ISDS provisions constitute an attack on states' sovereign immunity.

However, the truth is that ISDS is a conscious act of sovereignty. For a start, there is no breach of sovereign immunity, as nation states willingly give their advance consent to this form of adjudication through the proper validation of international agreements. Put simply, in the words of the United Nations, *"International arbitration is a voluntary and consent-based method of settling disputes... [and] advance consent to this form of adjudication, given by States in IIAs, solved the problem of sovereign immunity"*.¹¹⁴

In fact, there is nothing in ISDS arrangements that cannot be separately found in other legitimate legal instruments and procedures. First, arbitration itself is a commonly used form of adjudication outside national courts, present in commercial disputes as old as trade itself.¹¹⁵ In its core foundation, there is the mutual and voluntary consent of the disputing parties for an impartial, law-based approach to resolve conflicts.

Second, legal disputes between commons and sovereign national states constitute the central tenet of our civilised society. As set in stone by the Magna Carta, ‘*the King too should be bound by the law*’.¹¹⁶ And fortunately, in most contemporary societies, governments every day are legally and judicially held accountable for their acts.

In addition, outside the ISDS arena, there are myriad examples of sovereign states (including their domestic court decisions) being brought to international adjudication forums outside their domestic judicial

system with legally binding resolutions — e.g. the WTO Panel Proceedings, the European Court of Human Rights, the International Court of Justice.

What makes ISDS so unique — and yet no less legitimate — is the summation of these features in one single institution: that is, a set of legal rules governing an international arbitration forum to settle disputes between an investor and a sovereign state outside the domestic court system.

Myth 2: ISDS can overturn national legislation

Truth: ISDS tribunals do not have the authority to reverse national legislation or regulations

The most vitriolic — and yet misinformed — criticism against ISDS is the allegation that ISDS reduces the national ability to legislate domestic public policy.¹¹⁷ Unfortunately, this misconception was endorsed by the Productivity Commission Final Report on Bilateral and Regional Trade Agreements, which states “*ISDS provisions also created some risk for governments when making domestic policy decisions*”.¹¹⁸ If anything, investor-state arbitration constitutes an extra layer curbing government’s ability to *misregulate*.

Let’s be clear: there is no international investment agreement that allows ISDS tribunals to overturn national legislation or regulation.¹¹⁹ In contrast, most modern BITs unambiguously limit awards to non-punitive financial compensation and restitution of property.¹²⁰ For instance, all Australian ISDS-protected agreements since 2008 — which echo article 34 of the current US Model BIT — expressly state “*Where a tribunal makes a final award against a respondent, the tribunal may award, separately or in combination, only: (a) monetary damages and any applicable interest; and (b) restitution of property, in which case the award shall provide that the respondent may pay monetary damages and any applicable interest in lieu of restitution.*”¹²¹

The myth of ISDS adjudications mandating changes to national legislation is also not supported by evidence. A recent study commissioned by the Dutch government attests that 90% of ISDS cases are merely targeted to administrative acts (e.g. cancellation of licenses or permits), with the remaining 10% directed against general legislative measures “*hardly, if ever, successful*”.¹²² This finding is also reinforced by UNCTAD analysis, which states “*in practice [ISDS] tribunals rarely award non-monetary relief*”.¹²³ In any case, the United Nations agency is quite clear on how to eliminate any theoretical challenge to change national legislation (as done in the TPP final agreement and many other previous Australia’s international agreements): “*specifying in the IIA that the tribunal lacks that authority [to order the repeal or modification of domestic legislation] could prevent potentially costly and time-consuming arguments about the tribunal’s power in that regard*”.¹²⁴

The truth is that ISDS tribunals do not have the authority to overturn national legislation or regulations. Nonetheless *Myth 2* still lingers through false misrepresentations — see **Box 2: The Curious Case of ISDS vs. Minimum Wage Legislation in Egypt**.

Box 2: The Curious Case of ISDS vs. Minimum Wage Legislation in Egypt

Given the lack of evidence to support the myth that ISDS reduces the ability of a country to legislate domestic policy, critics have been quick to trumpet horror stories about the 'dangers' and 'unfairness' of investor-state arbitration. An illustrative case is represented by the 2012 ISDS proceeding of *Veolia Propreté vs. Arab Republic of Egypt* (ICSID Case No. ARB/12/15).

High-profile ISDS detractors — such as US Senator Elizabeth Warren and US presidential candidate Bernie Sanders — had accused the French company Veolia of using investor-state arbitration to prevent the Egyptian government from raising the minimum wage.¹²⁵ If true, this case would be the flagship exemplification of how intrusive ISDS provisions could threaten domestic public policy independence. However, this is yet another misrepresentation of ISDS cases.

Render unto Caesar what belongeth to Caesar

According to the contract signed between Veolia Propreté (a French waste management company) and the Egyptian city of Alexandria, any increase in operation costs outside the company's responsibility would have to be duly compensated. Nonetheless, at a later stage, the Egyptian authority raised the minimum wages, but failed to compensate the French firm in possible breach to its contractual obligations. As a result, the dispute eventually ended in an ISDS arbitral tribunal.

Most importantly, on no account did the French investor question the sovereign and democratic powers of the Egyptian government to set minimum wages, but only required that the original agreement be kept. That is, Veolia Propreté argued that such changes to employee compensation visibly amounted to an exogenous increase to its operation costs, and therefore the original price of the contract would need to be adjusted accordingly.

As of January 2016, the final arbitration ruling is still pending. However, no matter which party wins the case, the Egyptian government's ability to set its own minimum wage legislation has never been in question, and no ISDS award would be able to reverse the minimum wage hike, but only demand financial compensation for a specific contractual breach.

Moreover, even after recognising the implausibility of ISDS rulings effectively reversing national legislation, critics still point to concerns over regulatory chill. This is a situation where policy makers are discouraged from introducing new regulations due to fear of immense financial costs in potential ISDS award compensations.¹²⁶ Nonetheless, despite several anecdotes of alleged regulatory chill, empirical evidence for the phenomenon is still lacking.¹²⁷

First, ISDS does not impose regulatory chill any more than any other form of litigation in international forums (such as the WTO), or indeed, domestic courts. Regardless of ISDS provisions, most governments are already required to act in accordance to the law and the due process; irrespective of good public policy intentions, the end never justifies the means in a civilised society. In this way, ISDS is just another legal remedy to prevent unlawful government acts — in some cases, a very powerful and effective remedy, particularly in countries where the domestic rule of law environment is weak. If anything, "ISDS imposes a chill on government's ability to 'misregulate', that is, to act in an arbitrary, discriminatory, unfair, and inequitable manner".¹²⁸

Second, most modern BITs already include significant carve-outs to ISDS scope in order to avoid unnecessary regulatory chills.¹²⁹ For instance, Australia's Department of Foreign Affairs highlights a series of investor-state arbitration safeguards in the Trans-Pacific Partnership agreement, such as:

"There is explicit recognition that TPP Parties have an inherent right to regulate to protect public welfare, including in the areas of health

*and the environment; Australia's tobacco control measures cannot be challenged; certain ISDS claims in specific policy areas in Australia cannot be challenged, including: social services established or maintained for a public purpose, such as social welfare, public education, health and public utilities, measures with respect to creative arts, Indigenous traditional cultural expressions and other cultural heritage, Australia's foreign investment policy, including decisions of the Foreign Investment Review Board. Non-discriminatory regulatory actions to safeguard public welfare objectives, such as public health, safety or the environment, do not constitute indirect expropriation, except in rare circumstances; the fact that a subsidy or grant has not been issued or renewed, or has been reduced, does not breach the minimum standard of treatment obligation, even if it results in loss or damage to the investment. This includes subsidies issued under Australia's Pharmaceutical Benefits Scheme; government action which may be inconsistent with an investor's expectations does not constitute a breach of the minimum standard of treatment obligation, even if it results in loss or damage to the investment."*¹³⁰

In short, fears of regulatory chills or mandatory changes to national legislation are at best unfounded; at worst, a damaging misrepresentation.

Myth 3: ISDS gives special rights to foreign investors

Truth: ISDS simply provides the necessary means to enforce international treaty-based agreements in accordance to the rule of law

Another common libel against ISDS provisions concerns the allegedly special rights status given to foreign investors, which would be denied to domestic citizens. For instance, the Cato Institute's Daniel Ikenson states investor-state arbitrations "*turn national treatment on its head, giving privileges to foreign companies that are not available to domestic companies*".¹³¹ A few submissions to the Senate Inquiry on ISDS clauses also opposed these legal provisions for "*giving special preferential treatment to foreign investors compared with domestic investors*".¹³² Along the same lines, the Productivity Commission claims "*the general granting of additional substantive and procedural rights to foreign investors through ISDS can disadvantage domestic relative to foreign investments...*".¹³³

Overall, there are two specific arguments regarding alleged ISDS special rights status to foreign investors: one concerning procedural rights (that is, only foreign investors can access investor-state arbitration forums) and the other with respect to substantive rights (i.e. material safeguards). Both arguments are overstatements and should be refuted. The truth is that ISDS merely provides the necessary means for foreign investors to enforce international treaty-based agreements in accordance to the rule of law.

The ISDS procedural right granting foreign investors access to investor-state arbitration forums regards the specific legal nature of international investment

agreements (IIAs). Such IIAs are based on international law, and not always part of the domestic legal system.¹³⁴ As outlined by the European Commission, in such cases, international agreement legal provisions "*cannot be invoked before domestic courts, (which are competent to rule on disputes brought on the basis of national law)*. This is the *raison d'être* for international tribunals, including for investment matters".¹³⁵ Basically, these are international treaty-based matters well suited for an equally international law-based adjudication forum.

Further, there is the myth concerning ISDS special substantive rights. There is nothing in ISDS material protections that is not covered — or should not be covered — by a civilised society respectful of the rule of law: e.g. legal predictability, impartial adjudication, fair and equitable treatment, property rights, no unlawful discrimination, observance of contract obligations.¹³⁶ At the core of ISDS provisions is the right to *no expropriation without compensation*, which is a well anchored principle since the 1215 Magna Carta commandment: "*No freeman shall be... deprived of his freehold... unless by the lawful judgment of his peers and by the law of the land*";¹³⁷ and indeed consistent with the United Nations Universal Declaration of Human Rights;¹³⁸ the Protocol to the European Convention for the Protection of Human Rights and Fundamental freedoms;¹³⁹ and civil rights legislations across developed democracies, including the Australian Constitution.¹⁴⁰

Myth 4: ISDS should not be part of international agreements among developed countries

Truth: A patchwork collection of ISDS-protected agreements is counterproductive and undermined by treaty shopping conduct

An often — yet flawed — view claims ISDS provisions should not be part of treaties exclusively involving developed countries. The rationale is that domestic judicial systems in advanced democracies are fully able to provide for a safe and impartial rule of law environment, without the need for other alternative forms of adjudication such as investor-state arbitration. Such assessment was endorsed by the 2010 Productivity Commission Report on Bilateral and Regional Trade Agreements, which suggests as a solution to "*limit the application of ISDS to a subset of the member countries*", including "*time-limiting agreements...where one partner country is rapidly developing, such that its legal system can eventually resolve investment related disputes*".¹⁴¹

However, the same 'high-quality-legal-system' argument could be used to exempt disputes among developed countries from *any* form of international adjudication forum, including from the International Court of Justice or the WTO Panels. Yet past experience and theory show how important a neutral and de-politicised forum can be to effectively solve international disputes, even among developed nations with outstanding judicial systems.¹⁴²

In any case, there are still some important caveats to Myth 4's approach. First, a patchwork collection of ISDS-protected agreements can lead to perverse incentives for treaty shopping. As happened with the arbitral case involving Philip Morris Asia and the

Australian government,¹⁴³ some companies might attempt to use subsidiaries in other countries as proxies to pursue an investor-state arbitration solution — undermining not just the effectiveness of Australia's current 'case-by-case basis' approach, but the very legitimacy of ISDS provisions before the general public's eye.

Second, it constitutes a counterproductive discriminatory behaviour, forcing the Australian government of the day to an awkward position of publicly pointing out which trade partners are trusted or distrusted, using investor-state arbitration as last resource for damage control purposes.

Third, despite relatively high standards in the domestic judicial system, more and more foreign investors are choosing ISDS forums to pursue their claims against host governments in developed countries — even against the odds of an adverse outcome, where developed state

respondents are almost three times more likely to win than an investor claimant.¹⁴⁴

Indeed, one might argue that *Myth 4* skates on very thin ice: an unfounded self-serving assumption that developed countries provide a perfect (or quasi-perfect) rule of law environment. For instance, studies point out that *"Neither federal nor state law in the United States fully protects foreign investors against discrimination... There is also evidence that U.S. courts, especially civil juries, can exhibit biases against foreign investors"*.¹⁴⁵ In Australia, even the Productivity Commission — which once disavowed ISDS provisions between developed countries¹⁴⁶ — in a more recent study claimed our own legal system is *"too slow, too expensive and too adversarial"*.¹⁴⁷ Little wonder foreign investors facing idiosyncrasies, veiled discrimination and lengthy judicial processes in developed states are turning to ISDS forums.

Myth 5: ISDS is a redundant tool in international affairs

Truth: ISDS is an effective and unique tool to overcome political risks

Some critics often claim that ISDS is a redundant tool to overcome political risks, as there are many other options available for foreign investors to hedge their international operations.¹⁴⁸ For instance, the Productivity Commission suggests that investors should either seek political risk insurance — in private markets or in public shops such as the Australian Government's Export Finance and Insurance Corporation, and the World Bank Multilateral Investment Guarantee Agency — or directly negotiate a private contract with host governments for dispute resolution mechanisms.¹⁴⁹ However, there are some important forewarnings with such proposed ISDS substitutes.

First, due to potentially upfront high costs, such political risk insurance would not constitute a viable option for many international investors. As even the Productivity Commission recognises, such insurance markets are *"more feasible for large business rather than small and medium business"*.¹⁵⁰ Besides, this option would not necessarily prevent future litigation, as in many instances investors would still be forced to dispute with insurance companies on issues such as triggering clauses and amount awarded.

In addition, the notion that foreign investors could seek private contracts with host governments is misguided — and often unrealistic. As already pointed out, *"The notion that investors should protect themselves against foreign governments through contract rather than through investment treaties ignores the fact that most investments are private affairs in which no government is a party. Governments should not have free rein to*

expropriate (without fair compensation) property from parties that have no opportunity to bargain for this protection through contract".¹⁵¹

The truth is that ISDS is a unique legal provision offering an alternative neutral, law-based adjudication forum. Investor-state arbitration, as opposed to other forms of state-state disputes such as the WTO dispute settlement mechanism, or even armed conflicts and international sanctions, provides an independent, cost-effective and depoliticised environment.¹⁵² Hence, investors do not necessarily need to see their interests sacrificed by failing to gather support from their home state countries.

Another valuable feature in ISDS disputes is that arbitration allows the disputing parties (both investor claimant and state respondent) to exercise more control over the litigation procedure, including the choice of appointing highly-qualified experts to adjudicate the dispute.¹⁵³ Further, ISDS ruling enforcement is highly effective, with ICSID (the main ISDS arbitration forum, comprising two-thirds of all cases — see Figure II.2) reporting that the number of countries with known compliance issues had declined from six to just three in past years.¹⁵⁴

Overall, ISDS constitutes a legitimate alternative for dispute resolution. It accounts efficiently for political risks involving cross-border investments, and as explained by the UNCTAD, the appeal for investor-state arbitrations is *"motivated mainly by the perception that arbitration is swifter, cheaper, more flexible, and more familiar for economic operators"*.¹⁵⁵

Myth 6: There is no economic case for ISDS

Truth: ISDS promotes a global rule of law environment and cross-border investments

Another argument against investor-state arbitration resides in the claim that there is no economic case for ISDS provisions. According to this view, inclusion of ISDS clauses in international treaties would be justified only if there were severe and concrete menace to foreign investments. Yet according to some critics there is no such economic problem to be fixed. For instance, Simon Lester (2015) states that “*bad treatment of foreign investment is a problem of a prior era*”.¹⁵⁶ A similar view is supported by the Productivity Commission: “*There does not appear to be an underlying economic problem that necessitates the inclusion of ISDS provisions within agreements. Available evidence does not suggest that ISDS provisions have a significant impact on investment flows*”.¹⁵⁷ According to this assessment, contemporary political risks to foreign investments are limited and, in fact, already constrained by *reputational effects* — i.e. countries perceived to mistreat foreign investors would already be penalised with lower future capital inflows.¹⁵⁸

Nonetheless, there is plenty of evidence supporting the economic case for investor-state arbitration. First and foremost, by limiting unlawful government acts when it comes to foreign investment, ISDS promotes the rule of law across borders.¹⁵⁹ Since the primordium of the Magna Carta, a strong law-based society is fundamental to continuous social and economic development.¹⁶⁰

In this sense, the sharp decrease in expropriation of foreign investors in the past decades should not be seen

as a justification for ditching ISDS provisions, but indeed as a reflection of a better international law framework, of which bilateral investment agreements constitute a central part.¹⁶¹ Besides, unlawful government acts against foreign investments are far from confined to a bygone era, with the rising number of ISDS cases being a living proof that reputational effects alone will not hinder foreign investor mistreats.

Further, although there are many other factors influencing foreign direct investment (FDI), economic research indicates that investment-protection agreements may help promote cross-border investments.¹⁶² Hence, while BITs alone may not determine FDI decisions, ISDS-containing agreements effectively contribute to a better regulatory and institutional framework,¹⁶³ act as a proxy to the political commitment of host states towards foreign investors¹⁶⁴ and, in some cases, can function as a substitute for poor institutional quality.¹⁶⁵ All these features contribute toward a more conducive international investment framework, benefiting both importers and exporters of capital.

In short, contrary to the Productivity Commission’s and other critics’ claims, a porous global rule of law framework when it comes to foreign investment treatment constitutes an underlying and vivid economic problem, for which investment-protected agreements are well suited to cater.

Myth 7: ISDS benefits only big multinationals

Truth: ISDS cases are initiated by businesses of all shapes and sizes

A particularly unhelpful myth is that ISDS only benefits big multinationals.¹⁶⁶ As the Democratic US Senator Elizabeth Warren recently claimed, “*Agreeing to ISDS in this enormous new [TPP] treaty would tilt the playing field in the United States further in favour of big multinational corporations*”.¹⁶⁷ Likewise, Simon Lester from the Cato Institute claims that ISDS provisions are just intended to assist “*big corporations and rich investors*”.¹⁶⁸ In Australia, the Greens claim the ISDS-protected TPP negotiation process is ultimately driven by the “*interests of multinational companies*”.¹⁶⁹ However, despite widespread belief, such criticism is not backed by data.

While foreign investors are popularly thought of as ‘big business’, smaller firms use the ISDS system more often than larger ones: an OECD survey found that 22% of ISDS claimants are individuals and only 8% of the

companies concerned are multinational corporations;¹⁷⁰ a CSIS study concerning US investors shows that two-thirds of ISDS claimants were either individuals or small and medium-sized enterprises with fewer than 500 employees;¹⁷¹ in another evidence-based research on a large sample of public ISDS concluded cases, more than 90% of claimants were outside the Financial Times 500 large corporation (FT500) ranking.¹⁷²

Therefore, as evidence shows, it is mutually beneficial for both small and bigger investors to create an effective mechanism to the protection of foreign investments. In this regard, ISDS provisions empower foreign investors of all stripes to pursue their claims without the need to align them with their home state’s interests — indeed, a particularly daunting task for individual entrepreneurs and small businesses.



Conclusion

This report debunks the widespread and unfounded myths about investor-state arbitration, showcasing it as a beacon for the rule of law in international affairs. ISDS provisions constitute a conscious act of sovereignty, with nothing in the arrangements that cannot be separately found in other legitimate legal instruments and procedures. At the core of ISDS provisions is the right to *no expropriation without compensation*, which is a well anchored principle in many foundational legal documents, from the Magna Carta to the United Nations Universal Declaration of Human Rights to many other civil rights legislations across developed democracies, including the Australian Constitution.

Since the first ISDS-protected international treaty signed in 1959 between Germany and Pakistan, investor-state arbitration has become a legal reality to over a hundred nations worldwide — with currently more than 3,000 bilateral agreements formally backing the right of foreign investors to hold host states accountable for unlawful treatment. Among many benefits, the spread of investor-state arbitration has proved an effective non-belligerent alternative to state-to-state dispute escalation, providing a safer environment for international investment as well as further ammunition for local forces towards a law-based democratic system.

Trailing accelerated international capital flows since the end of the Cold War, the rise of ISDS claims has been in tandem with globalisation. From just under 100 cases initiated before 2003, the total amount of known investor-state arbitral disputes has grown to more than 600 cases at present. Such a rapid increase in disputes is evidence that investor-state arbitration remains an attractive option for a neutral, law-based and depoliticised adjudication forum — even in developed host

states — providing an international fair play environment for entrepreneurial activities of all shapes and sizes.

In addition, the rise in jurisprudence also offers valuable lessons for a better design of ISDS clauses: transparency of proceedings, *amicus curiae* submissions, binding interpretations, tightened statutes of limitations, proper guidelines on indirect expropriation assessments, and sensitive regulatory area exemptions are all new features assimilated in recent international agreements in order to ensure a legitimate and well-tailored use of investor-state arbitration. This is proof that the system is responsive to valid concerns, and able to perfect itself to maintain fit for purpose despite constantly-changing challenges.

With ISDS provisions in 21 bilateral treaties and seven free trade agreements, investor-state arbitration has served Australia's national interests well, promoting a better global rule of law environment along with protecting Australian investors from unlawful foreign government acts. Hence, it is time to advance our commitment to this important international tool: i.e. Australia must reconsider its current 'case-by-case basis' approach and move towards fully embracing ISDS provisions, advocating for a transparent, well-delimited and legitimate use of investor-state arbitration. Moreover, Australia should maintain its international efforts to implement an ISDS appellate mechanism, and whenever possible, to work with its trading partners to ensure that previous ISDS commitments are updated and fit for purpose.

There is nothing to fear from investor-state arbitration and much to welcome it in our international commitments. And that's the beauty of the rule of law: those who owe nothing have nothing to fear — and much to gain.



Appendix: The ISDS Cases involving Australian Investors and Government

White Industries Australia Limited v. The Republic of India

On 30th November 2011, a three member *ad hoc* tribunal¹⁷³ under UNCITRAL arbitration rules rendered the first published ISDS award against India — and the first involving an Australian investor claimant — in *White Industries Australia Limited v. Republic of India*.¹⁷⁴ The arbitral tribunal held that India's unreasonable delay in enforcing an earlier arbitral award granted to White Industries Australia Limited (White Industries) violated the effective means standard¹⁷⁵ incorporated by the most-favoured nation provision of the 1999 Australia-India bilateral investment treaty. As a result, the Australian company was awarded the amount due in the original award of AU\$4.8 million plus interest.¹⁷⁶

Essential facts of the case

In 1989, White Industries entered into an eight-year contract with Coal India Limited (Coal India), a state-owned enterprise, for the supply of equipment and development of a coalmine in the Indian state of Bihar. A dispute arose over bonus and penalty payments, as well as over the quality of coal extracted, prompting White Industries to commence arbitral proceedings under International Chamber of Commerce (ICC) rules in 1999. Eventually, an AU\$4.8 million award was granted by the ICC Tribunal to White Industries in May 2002. Later that year, Coal India applied to the Calcutta High Court to have the award set aside under the 1996 Indian Arbitration and Conciliation Act, while White Industries concurrently applied to the New Delhi High Court to enforce the ICC Award in India. Both proceedings experienced significant delays, with enforcement pleas still pending before the Indian Supreme Court.¹⁷⁷

After years of delay and effort to have the original ICC award enforced, White Industries commenced

arbitration against India in 2010 in accordance with the India-Australia BIT, claiming the inordinate delay violated articles 2, 3 and 9 of the bilateral agreement in a breach of the provisions on fair and equitable treatment, expropriation, the effective means standard incorporated by the most favoured nation clause, and free transfer of funds under the treaty. India denied each of the alleged BIT breaches and argued, in addition, that the arbitral tribunal did not have jurisdiction to hear this claim as White Industries could not be considered a proper international investor in India, and none of the assets on which it relied as constituting investments into India qualified as such under Article I of the BIT.¹⁷⁸

Australian Investor awarded compensation

The UNCITRAL tribunal dismissed White Industries allegations relating to the violation of fair and equitable treatment, expropriation, and free transfer of funds under the BIT. However, on 30th November 2011, the arbitral court ruled that India had violated the India-Australia BIT because lengthy delays in enforcing the ICC Award breached the effective means standard imported through the most favoured nation (MFN) clause. According to the decision, through the MFN clause, White Industries could invoke India's obligation to provide investors with "*effective means of asserting claims and enforcing rights*" contained in the 2001 Kuwait-India BIT, even though the Australia-India BIT did not include such an obligation for host states.¹⁷⁹ As a result, the Australian company was awarded the full amount due in the original award plus interest.¹⁸⁰

Planet Mining Proprietary Limited v. Republic of Indonesia

On 22nd June 2012, the Australian-based Planet Mining Proprietary Limited, together with its British parent company Churchill Mining, registered a claim for arbitration against the Republic of Indonesia.¹⁸¹ The claim cited a breach of the 1992 Australia-Indonesia BIT and the 1976 United Kingdom-Indonesia BIT due to a licensing dispute in which competitors were also granted licenses that overlapped a substantial area of the East Kutai Coal Project to which Planet Mining and Churchill Mining believed they had exclusive rights. Planet Mining and Churchill Mining also disputed Indonesian authorities' decision to revoke their mining licenses in 2010.¹⁸²

After failure to reach an agreement, a three-panel *ad hoc* tribunal was constituted on 3rd October 2012 under ICSID Rules, comprised of Gabrielle Kaufmann-Kohler as President, Michael Hwang appointed by Indonesia, and Albert Jan Van Den Berg appointed by Churchill Mining and Planet Mining. Data on the specific nature of alleged breaches remains confidential¹⁸³ with a final decision on arbitral proceedings still pending.¹⁸⁴

Essential facts of the case

Between 2005 and 2010, PT Indonesian Coal Development, in conjunction with other affiliated Indonesian mining companies, developed the East Kutai Coal Project. During the development stage, Churchill Mining and Planet Mining acquired PT Indonesian Coal Development in 2006, and between 2007 and 2009, Churchill and Planet Mining's Indonesian partners were granted licenses to conduct surveying and exploration of the East Kutai Coal Project region.

At the same time, Indonesia granted exploration licenses to the other competitors, allowing them access

to an overlapping area of the Coal Project.¹⁸⁵ In addition, the Indonesian authorities revoked the licenses held by Churchill and Planet's Indonesian partners in May 2010. Disputing these measures and failing to reach an agreement with the Indonesian authorities, Churchill Mining and Planet Mining filed for ISDS arbitration under ICSID rules in June 2012.

A key preliminary issue of the case became establishment of the standard for finding Indonesia's consent to arbitration. The ICSID tribunal found that the consent clause in the Australia-Indonesia BIT required a further separate act, which was in fact crystallised in regulatory approvals by the words "*shall consent in writing ... within forty five days*" of the Australia-Indonesia BIT. This wording was also included in the Indonesian Investment Coordinating Board's 2005 approval which authorised the PT Indonesian Coal Development to mine in the East Kutai Coal Project region. In addition, the tribunal found a standing consent clause to arbitration in the United Kingdom-Indonesia BIT.¹⁸⁶ Indonesia's consent to arbitration under each of the Australia-Indonesia and United Kingdom-Indonesia BITs was further recognised as pursuant to the general rules on treaty interpretation found in Articles 31-32 of the Vienna Convention on the Law of Treaties. In both cases, the tribunal also found that the investments had been granted admission in accordance with the relevant Indonesian law pursuant to both BITs.¹⁸⁷

Final decision still pending

With arbitral jurisdiction and Indonesia's consent to arbitration established, a decision on specific breaches of BITs and final awards are yet to be reached, with a total of US\$1.3 billion being claimed cumulatively between Planet and Churchill Mining.¹⁸⁸

Tethyan Copper Company Pty Limited v. Islamic Republic of Pakistan

On 19th October 2011, the Australian-based Tethyan Copper Company Proprietary Limited (Tethyan Copper) submitted a response to the Baluchistan Government of Pakistan claiming the expropriation of its investments was in breach of Article 7 under the 1998 Australian-Pakistan BIT.¹⁸⁹ Failure to reach agreement led to ISDS proceedings with a three panel *ad hoc* tribunal constituted on 12th July 2012 under ICSID arbitration rules.¹⁹⁰

The compensation amount claimed by Tethyan Copper remains confidential and the status of proceedings is currently pending, with the Government of Pakistan filing a reply on Tethyan Coppers' application to dismiss the claims on 10th November, 2015.¹⁹¹

Essential Facts of the Case

In 1993, BHP Minerals International Exploration Inc. and the Baluchistan Development Authority entered into the Chagai Hills Exploration Joint Venture Agreement (CHEJVA) to explore for deposits of gold, copper, and other minerals in the Chagai district of Baluchistan. In April 2006, Tethyan Copper acquired the contract from BHP Minerals, becoming party to the venture through a novation agreement with the Government of Baluchistan and BHP.¹⁹²

In February 2011, Tethyan Copper submitted an application for a mining lease for a portion of Reko Dig situated within the boundaries of the license originally granted to BHP under CHEJVA. The application was

supported by a feasibility study and appropriate documents in accordance with the Baluchistan Government's Mineral Rules. On 15th November 2011, the government authority denied the application.¹⁹³

Following a failed effort at conciliation between the parties, Tethyan Copper filed for arbitration proceedings under ICSID Rules claiming expropriation of its investments and requesting the Tribunal appoint provisional measures that restrained the Government of Baluchistan from taking any steps to develop, sell, lease, and transfer Reko Dig mining area and from breaching the confidentiality provisions of Tethyan Copper Company's feasibility study.¹⁹⁴

Final decision still pending

The Tribunal recognised jurisdiction for the case under Article 13 of the Australia-Pakistan BIT and Article 25 (1) of ICSID Rules, as well as the authority to order

provisional measures under Article 47 of the ICSID Convention.¹⁹⁵ Tethyan Copper successfully proved at first appearance that it owned a legally protected interest, however the Tribunal ruled there was insufficient evidence to show that provisional measures were necessary to avoid irreparable harm, and thus the claim for provisional measures was rejected. Instead, the Tribunal observed that Pakistan was required to inform of any changes of intent regarding the implementation of the mining area work plan, any plans to expand its mining activities to other sections, and any deposit encompassed by the original license. Pakistan was also instructed to refuse rights of the mine to any third party and to refrain from breaching the confidentiality provisions of Tethyan Copper's feasibility study, infringing Tethyan Copper's exclusive surface rights under the Surface Rights Lease, aggravating the dispute or rendering ineffective any ultimate relief granted by the Tribunal.¹⁹⁶ A decision on compensation is yet to be announced.

Philip Morris Asia Limited v. The Commonwealth of Australia

On 21st November 2011, Philip Morris Asia Limited (Philip Morris Asia) filed a claim for arbitration under UNCITRAL Rules against Australia in *Philip Morris Asia Limited v. The Commonwealth of Australia*.¹⁹⁷ Philip Morris Asia held that Australia's plain packaging laws on cigarettes were in violation of Australia's commitments under the 1993 Agreement between the Government of Hong Kong and the Government of Australia for the Promotion and Protection of Investments (Australia-Hong Kong BIT).

Under a series of claims, Philip Morris Asia argued Australia's 2011 Plain Packaging Act legislation constituted unlawful expropriation in breach of Article 6 of the Australia-Hong Kong BIT. In addition, the company contended the legislation infringed Australia's commitment under Article 2(2) of the Hong Kong Agreement in two accounts. First, that the Plain Packaging Act failed to accord fair and equitable treatment to Philip Morris Asia's investments, and that such legislation also constituted an unreasonable and discriminatory measure depriving Philip Morris Asia's investments from full protection and security. Australia rejected all these claims, including that the arbitral court lacked jurisdiction and admissibility to hear the claim.¹⁹⁸

On 17th December 2015 the arbitral tribunal in Singapore dismissed the case, agreeing with Australia's position that the tribunal had no jurisdiction or admissibility to hear Philip Morris's claim.

Essential Facts of the Case

In April 2012, two challenges to the tobacco plain packaging legislation were heard by the High Court of Australia: *British American Tobacco Australasia Limited and Ors vs. Commonwealth of Australia*, and *Japan Tobacco International SA vs. Commonwealth of Australia*. On 15th August 2012, the High Court found that the Tobacco Plain Packaging Act 2011 was not contrary to the Constitution. By a 6:1 majority the Court held "there had been no acquisition of property that would have required provision of 'just terms' under section 51(xxxi) of the Constitution".¹⁹⁹

Instead of seeking reparation through Australian domestic courts as its tobacco industry competitors had, Philip Morris headquarters decided to take a different route. On 23rd February 2011, following announcements from the Australian Government intention to introduce a legislative bill on tobacco plain packaging, Philip Morris International arranged for its wholly-owned Hong Kong subsidiary, Philip Morris Asia, to take over its two Australian subsidiaries, Philip Morris Australia Limited and Philip Morris Limited. Then in June 2011, Philip Morris Asia placed a notice of claim seeking amicable settlement under the Australia-Hong Kong BIT. After frustrated negotiations with the Australian Government, a formal claim for arbitration was filed on 21st November 2011 under UNCITRAL Rules.

The First Procedural Meeting was held in July 2012 in Singapore with an *ad hoc* three-person arbitral tribunal comprised of Professor Don McRae of the University of Ottawa as Australia's appointee, Professor Gabrielle Kaufmann-Kohler as Philip Morris's appointee, and with Professor Karl-Heinz Böckstiegel appointed as the presiding arbitrator by the Secretary-General of the Permanent Court of Arbitration.

In response to the Notice of Arbitration, Australia argued that Article 10 of the Australia-Hong Kong BIT did not afford jurisdiction for an arbitral tribunal to preside over previous disputes re-packaged as BIT claims after a government has passed relevant legislation. In addition, Australia argued its plain packaging policy could not breach protections provided under the BIT because Philip Morris made the decision to acquire shares in Philip Morris Australia in full knowledge of Australia's intention to implement plain packaging legislation. Moreover,

Australia asserted that an investor could not "*make out a claim for breach of (say) the fair and equitable treatment standard or of expropriation in circumstances where (i) a host State has announced that it is going to take certain regulatory measures in protection of public health, (ii) the prospective investor — fully advised of the relevant facts — then acquires some form of an interest in the object of the regulatory measures, and (iii) the host State then acts in the way it has said it is going to act*".²⁰⁰

Arbitration Case Dismissed

On 17th December 2015 the arbitration case was dismissed in agreement with Australia's position on the grounds that the arbitral court lacked jurisdiction and admissibility to hear the claim. The tribunal's detailed reasoning for rejecting jurisdiction is not yet known.²⁰¹

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