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Possible reform of Investor-State dispute settlement (ISDS)

Submission from the Government of the Russian Federation

Note by the Secretariat

This note reproduces a submission received on 31 December 2019 from the Government of the Russian Federation in preparation for the resumed thirty-eighth session of the Working Group. The submission is reproduced as an annex to this note in the form in which it was received.

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Annex

Draft

Statement
of the Russian Federation
on specific initiatives within the framework of UNCITRAL
in relation to the reform of investment arbitration

I. General comments

1. The Russian Federation welcomes the initiatives proposed by various States within the framework of Working Group III with a view to reform of the investor-State dispute settlement (ISDS) system.

2. This document sets out the preliminary reflections of the Russian Federation with regard to the initiative proposed by a number of UNCITRAL member States to establish an international investment court.

3. According to document A/CN.9/WG.III/WP.159/Add.1,[1] the establishment of a permanent international investment court would, inter alia, ensure the consistency and predictability of rulings on investment disputes, resolve concerns relating to decision makers and reduce the costs borne by the parties to investment disputes.

4. This idea is seen by its authors as a kind of ultima ratio that would supposedly resolve or allay most of the concerns identified by Working Group III with respect to the ISDS system. However, the Russian Federation considers that the establishment of an international investment court is highly likely to have the opposite effect, leading to new problems in the handling of investment disputes and at the same time failing to overcome the existing shortcomings of the ISDS system.

I. The current system's advantages, the loss of which would make ISDS less attractive to States and investors

5. The arbitration model for dispute settlement offers advantages that would be lost if disputes were referred to a permanent investment arbitration court. Such advantages include the right of the parties to proceedings to choose the arbitrators, which ensures confidence in the current ISDS system and the flexibility of procedural rules that make it possible to take into account the specificities of each dispute.

(1) Involvement of States and investors in the process of appointing decision makers

6. The direct involvement of the parties to a dispute in the selection of decision makers enables the parties to take into account many factors that are important to them. This ultimately determines the degree of confidence among parties to disputes, and among the wider public, in the arbitration mechanism for dispute resolution.

7. However, the international investment court model would preclude the selection by parties of decision makers to handle specific cases, involving instead the appointment by States of permanent judges.

8. Thus, regardless of the modalities of such an international investment court, the possibility of investors' involvement in appointing members of the tribunal would be ruled out entirely. The possibility for investors and States to select a panel of persons to examine their case would also be precluded. As a result, the trust of not only States but also investors, as beneficiaries of the guarantees provided by investment treaties, in the ISDS system may be undermined. The

[1] Paras. 40–56.

perception of an international investment court as an instrument depriving investors acting in good faith of the possibility to participate in the selection of the applicable procedure may have a negative impact on the implementation of investment projects in host countries and lead to a radical transformation of the established investment protection model.

9. For the reasons given above, the establishment of an international investment court might appear to offer a comprehensive solution but in reality would entail procedural changes that would not help to resolve the concerns discussed in Working Group III.

(2) The availability of options for optimizing the dispute settlement process

10. Currently, participants in proceedings may select the procedural rules applicable to examination of the dispute, determine whether the proceedings will be confidential and whether they should include a disclosure phase, choose the language of the proceedings and determine the place and format of the arbitration.

The establishment of a permanent international investment court would entail the uniformity and, to a large extent, the elimination of such procedural possibilities.

Loss of the flexibility of the dispute settlement model would not only make proceedings less convenient; it might also have a negative impact on their cost and duration. Among other things, the parties could face additional costs for translation and interpretation, as they would be limited in their ability to choose the language appropriate to the proceedings. This, in turn, would lead to lengthier proceedings and thus an increase in the financial costs borne by the parties.

11. Moreover, in many investment arbitration proceedings (except in the case of arbitration at the International Centre for Settlement of Investment Disputes (ICSID)), the choice of the jurisdiction in which the dispute will be handled and, accordingly, of the courts competent to rule, inter alia, on the setting aside of awards, is crucial. The establishment of an international investment court would mean that, in effect, the seat of the court would exercise a monopoly on jurisdiction or the question of jurisdiction would be eliminated altogether, thus depriving parties to a dispute of their right to choice of jurisdiction. Furthermore, the recognition and enforcement of arbitral awards in accordance with the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 reflect an important component of the sovereign right of States to monitor compliance with the principles of public policy in their territory, including with respect to the protection of human rights and fundamental freedoms and environmental safety.

II. Shortcomings of the current ISDS system, as identified by Working Group III, that cannot be resolved definitively or effectively

12. The establishment of an international investment court would not effectively address the concerns identified by Working Group III and referred to in document A/CN.9/WG.III/WP.149 with regard to the existing ISDS system. With respect to the concerns relating to the consistency, coherence, predictability and correctness of arbitral decisions, the inconsistency of decisions would persist. Costs relating to advisers would continue to be significant and the caseload of the court would be high.

(1) Uniformity of judicial practice would not be guaranteed

13. Proponents of the establishment of an international investment court assume that the court would establish unambiguous and consistent practices.[2]

[2] A/CN.9/WG.III/WP.159/Add.1, paras. 41–45.

However, the conditions under which it is proposed to establish the new court are different from those under which existing permanent international courts and tribunals were established and currently operate. Those courts and tribunals interpret specific provisions of certain international treaties, whereas the resolution of investment disputes in each case requires the application of one of more than 3,000 international investment treaties, which often contain different provisions.

14. In such situations, it is not possible to achieve uniformity in procedural methods, since:

1. Difficulties with respect to uniform interpretation may arise even in relation to a single provision of a sole international treaty, let alone in relation to many different international investment treaties.

2. Similar or even identical provisions in international treaties may have different meanings, depending on the rules of interpretation (for example, where travaux préparatoires are referred to).

3. The circumstances of the dispute differ significantly from case to case (a single action by the respondent State may have different economic and social grounds and, as a result, lead to contrasting conclusions when the conformity of that action with the investment agreement is assessed).

4. The decision of an international investment court would be binding only on the parties to the proceedings and the impact of such a decision on rulings with respect to other disputes would therefore be limited, as under the current system.

(2) A new parallel legal regime would intensify the fragmentation of international investment law

15. Proponents of the establishment of an international investment court believe that it is possible to create a single specialized forum for ISDS.

However, there is little likelihood that the jurisdiction of an international investment court would extend to all existing international treaties.

The proposal for the establishment of such a court has been met with varying responses among States; some do not support it, while others remain cautious. Consequently, many States may defer the inclusion in their international investment treaties of clauses providing for the possibility of recourse to a permanent international investment court, at least until the effectiveness of such a mechanism has been confirmed (if indeed it is confirmed). An arbitral system of dispute resolution would continue to exist in parallel with the court, a situation that would not, as claimed, lead to the harmonization of investment dispute settlement.

16. Moreover, the proposed court would be competent to handle disputes arising after a dispute settlement agreement had been concluded or after a reservation to an existing agreement had been negotiated. Thus, a lengthy transition period during which investment arbitration courts would retain their jurisdiction would be inevitable.

17. Such a situation, in which several legal regimes would exist in parallel, would only increase the fragmentation of international investment law and create even greater legal uncertainty with respect to the application and interpretation of investment agreements.

(3) The diversity of decision makers would not be ensured

18. In addition to the issues highlighted above with respect to decision makers – issues that would not be resolved by the proposed procedural methods – there is the problem of the lack of diversity among decision makers. The current system for investment dispute settlement is often criticized for the closed nature of the

circle of arbitrators and the difficulty of renewing the core pool of arbitrators involved in most proceedings.

19. However, the model of a permanent international investment court with a fixed number of judges would further limit the current possibilities for participating States to bring new practitioners into the ISDS system, ensure equitable geographical representation of decision makers and appoint, for the examination of specific disputes, persons with the knowledge and qualifications sought by the parties and pertinent to the specific nature of the dispute in question.

It is assumed that appointments would be made by the same body or persons,[3] a situation that would also, in practice, prevent greater diversity among adjudicators.

Thus, the referral of disputes to an international investment court would be likely to create obstacles to, rather than helping to ensure, balanced representation.

(4) Costs would continue to be high

20. Currently, investment disputes are expensive in terms of legal costs, which include arbitrators' and advisers' fees and the fees charged by the institution administering the arbitration.

The financing of the international investment court would not relieve the parties of the need to pay for legal advice, which, according to experts, can account for up to 90 per cent of the total cost of the proceedings.[4] Other costs – arbitrators' fees and the fees charged by the institution administering the arbitration – would continue to apply but would be referred to by a different name, and would probably be borne only by States, even those that had joined the court but were not, in practice, parties to proceedings before it.

It is therefore unlikely that the establishment of an international investment court would significantly reduce any of the costs in question.

(5) The caseload of the system would determine the duration of the proceedings

21. The current ISDS system is criticized for failing to ensure optimal time frames for ISDS, including in the context of an increasing number of disputes.[5]

Through the creation of an international investment court, it is envisaged that the procedure for initiating cases against States will be simplified, including through the establishment of a small fee for the investor to file a case with the court.[6]

Such a mechanism may give impulse to at least two trends. Firstly, it is highly probable that the number of claims against States, including frivolous claims, would greatly increase. Moreover, even if the mechanism for the early dismissal of frivolous claims were to work effectively, the burden on the international investment court could be enormous. Such a development would have a negative impact on both the duration and the cost of ISDS proceedings, not to mention the size of the budget of the court itself and the number of its staff.

22. Secondly, the proposed system would not encourage the out-of-court settlement of disputes, which is preferable as it not only resolves the problem of duration and cost but also preserves the relationship between the investor and the State, ensures the smooth implementation of investment projects and enhances the reputation of States among foreign investors.

[3] A/CN.9/WG.III/WP.185, para. 55.
[4] A/CN.9/930/Rev.1, para. 36.
[5] A/CN.9/WG.III/WP.185, paras. 54–59.
[6] A/CN.9/WG.III/WP.185, para. 65.

It should also be noted that one of the reasons for the excessive length of dispute settlement proceedings is the heavy caseload of the "first tier" of arbitrators, whose schedule is often set for several years ahead. However, as indicated above, the establishment of a permanent body of judges would preclude any possibility of choice of decision makers. In other words, there would no longer be any real possibility of expediting the proceedings by selecting new adjudicators who could commence their examination of the dispute at the earliest possible time.

III. New challenges that would add to the list of problems presented by the ISDS system

23. A permanent international investment court would not meet the needs of States and investors, particularly in terms of optimal composition of the tribunal, low-cost solutions and fair distribution of the financial burden.

(1) Number of judges

24. Arbitral tribunals handle a significant number of investment disputes yearly.[7] This raises the question of the number of judges needed and the number of cases that those judges would realistically be able to consider each year.

25. The consideration by a small number of judges of a large number of cases would result in lengthier proceedings and consequent economic losses for both States and investors. In the event of a significant number of cases before the permanent international investment court and a resulting increase in the number of judges required to cover the additional workload, it would be difficult to predict the growth of the court's budget. In such a situation, the high number of judges would defeat the objective of consistency of decisions and practice.

(2) The budget of the court

26. The budget of the international investment court would include, at a minimum, judges' salaries and social security payments and the salaries of the court secretariat and other staff.

In order to ensure the high qualifications, independence and impartiality of the judges of the permanent international investment court, it would be necessary to provide those judges with a decent salary. It would also be necessary to provide for the payment of social benefits to the judges and for other guarantees, privileges and immunities to ensure their independence. Consequently, the size of these items of the court's budget would be large indeed.

27. The costs of financing the secretariat of the international investment court and payment for the services of secretaries and (if any) experts of the court would also form a significant part of the budget. The proposed framework for the establishment of the court does not take these costs into account.

28. In order to meet the growing demands of ISDS participants, it is likely that regular upward revisions of the court's budget would be required.

For example, the budget of the International Criminal Court increased from 30 to 144 million euros per year between 2002 and 2017, reaching 148 million euros in 2019.[8] The budget of the European Court of Human Rights in 2019 was almost 70 million euros.

Thus, it is not possible to estimate objectively all possible costs arising from the operation of the court, to establish with any certainty the amount of States' contributions to its operation or to state with confidence that the costs borne by States in ensuring the functioning of the ISDS system would decrease.

[7] https://investmentpolicy.unctad.org/investment-dispute-settlement.

[8] https://asp.icc-cpi.int/iccdocs/asp_docs/ASP16/ICC-ASP-16-11-ENG.pdf.

(3) Sharing the burden of maintaining the court

29. It is envisaged that the financial burden on participants in the ISDS system would be reduced through the distribution among participating States of fixed costs constituting the budget of the international investment court.

However, the soundness of an approach whereby the court would be financed by States not involved in any judicial proceedings during the financial year, or whose investors would not need to apply to that court, is questionable.

IV. Conclusions

30. The existing ISDS system is not without shortcomings, but those shortcomings can be overcome through consistent efforts to address the specific problems that have been identified, which would be a more effective approach than adopting radical solutions that are claimed to be universally applicable but in reality would not resolve the issues identified. Such initiatives as the establishment of an international investment court, despite their global nature, fail to address the substantive aspects of the problems identified, instead focusing on new ways of maintaining the status quo, which is hardly likely to achieve concrete results in the foreseeable future.

31. In view of the above, the Russian Federation considers that the initiative to establish an international investment court does not offer such advantages as to warrant its selection as a preferred solution. On the contrary, a permanent international court would at best become yet another link in the chain of problems afflicting the ISDS system and at worst a heavy burden under the weight of which the entire system for the settlement of international investment disputes would crumble.

32. The Russian Federation proposes that the advantages of the current system for the settlement of investment disputes be preserved and that efforts focus on resolving the identified problems arising from that system. Such an approach will ensure the optimal use of Working Group III resources while maintaining the effectiveness of the work carried out, and will also ensure that the principle of consensus in decision-making is upheld.