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Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-fourth session (Vienna, 27 November–1 December 2017)

Part II*

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* Part I of this Report is contained in A/CN.9/930/Rev.1.

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IV. Possible reform of investor-State dispute settlement (*continued*)

4. Other procedural issues

Early dismissal mechanism

1. The Working Group recalled its discussion of concerns stemming from the lack of an early dismissal mechanism to deal with unfounded claims — that is, unmeritorious, frivolous and abusive claims (see para. 39 of A/CN.9/930). The importance of those concerns from a legitimacy perspective was highlighted. Accordingly, it was agreed that there was merit in considering the possible provision of an early dismissal mechanism in ISDS.

2. In that context, it was also noted that such consideration should take into account existing mechanisms that had been developed by States (as well as in the ICSID Arbitration Rules) to provide for early dismissal and that the focus of the work should be on addressing circumstances where such mechanisms were not yet in place. It was added that other issues should be borne in mind, including possible barriers to access to ISDS (see para. 59 of A/CN.9/930), which might increase the risk of unfounded claims. It was suggested that claims by shell companies, other abusive procedures and inflated or unsubstantiated claims, which might not be considered unfounded claims per se but had the potential to increase duration and costs, should also be brought into consideration at a later stage.

Counterclaims

3. The Working Group undertook a consideration of the question of the limited ability of respondent States to make counterclaims in ISDS. Noting that that issue was closely related to the substantive obligations in investment treaties, a suggestion was made that the Working Group should not address the topic, as it had decided that its work should focus on the procedural aspects of dispute settlement rather than on the substantive provisions in investment treaties (see para. 20 of A/CN.9/930).

4. It was added that provisions permitting counterclaims were provided for in recent investment treaties. Certain arbitration rules, such as Rule 40 of the ICSID Arbitration Rules on ancillary claims, also provided for such a possibility. It was underlined that the main issue arose from the fact that investment treaties were generally formulated to provide protection to investors. As the latter had limited reciprocal obligations, the respondent States did not have a basis to bring a counterclaim. It was further mentioned that the basis for counterclaims might be and were often included in investment contracts, which then raised other practical difficulties not only with respect to the jurisdiction of the forum but also to the applicable law (public international law/domestic law). A cautious approach was suggested, given that there might be drawbacks in undertaking work in that area.

5. A different view was that providing a mechanism for States to raise counterclaims was an important aspect of ensuring an appropriate balance between respondent States and claimant investors as well as for promoting procedural efficiency, fairness and the rule of law. It was mentioned that allowing States to raise counterclaims could eliminate parallel proceedings and thus might have a positive impact on duration and costs as well as on a number of other procedural issues, including third-party funding.

6. While an approach taken by some arbitral tribunals happened to accept jurisdiction to address counterclaims in reliance on substantive obligations in investment treaties, it was reiterated that the nature of the substantive obligations themselves was not the focus of the Working Group. It was noted that there was a distinction between substantive obligations provided for in investment treaties and the dispute settlement mechanisms used to enforce those obligations.

7. After discussion, the general understanding was that any work by the Working Group would not foreclose consideration of the possibility that a State might bring a counterclaim where there was a legal basis (or an underlying provision) for so doing.

Account to be taken of ongoing reforms

8. It was widely felt that any reform of ISDS procedure should take into account ongoing States' reforms of the underlying treaties. Accordingly, it was suggested that provisions in more recent treaties on procedural matters in dispute settlement might inform the future deliberations of the Working Group. Such procedural matters, it was added, sought to address some concerns discussed earlier in the session. Indeed, more recent treaty provisions also included procedures to address subject-matter specific claims, and the relief that arbitral tribunals could grant.

5. Outcomes: coherence and consistency

9. The Working Group undertook its consideration of coherence and consistency in ISDS outcomes, based on document A/CN.9/WG.III/WP.142, paragraphs 31 to 38.

10. At the outset of the deliberations, it was noted that a coherent system would ensure that its components were logically related with no contradictions and that a consistent system would ensure that identical or similar situations were treated in the same manner. In that context, a distinction was made between circumstances in which inconsistent interpretations might be justified due to, for example, variations in the language of the investment treaties and circumstances in which such inconsistencies would not be justified, as the same measure and the same underlying treaty provision were being addressed. Similarly, the need to distinguish between achieving consistency of interpretation within the same investment treaty and consistency of interpretation across investment treaties was highlighted.

11. Acknowledging the importance of ensuring a coherent and consistent ISDS regime as described in paragraph 31 of A/CN.9/WG.III/WP.142, it was said that such a regime would support the rule of law, enhance confidence in the stability of the investment environment and further bring legitimacy to the regime. It was also said that inconsistency and lack of coherence, on the other hand, could negatively affect the reliability, effectiveness and predictability of the ISDS regime and, in the longer term, its credibility and legitimacy. It was mentioned that criticism of a lack of consistency and coherence was one of the reasons behind the Commission's decision to embark on work on possible ISDS reform. It was underlined that consistency was a crucial element of the rule of law and would contribute to the development of investment law. However, it was also noted that consistency and coherence were not objectives in themselves and extreme caution should be taken in trying to achieve uniform interpretation of provisions across the wide range of investment treaties.

12. Yet another view was that the discussions should fully take into account the historical background of ISDS as an effort to provide investors a neutral mechanism to resolve their disputes with States.

13. The fragmented nature of the underlying investment treaties, as well as the ad hoc nature of arbitration, in which individual tribunals were tasked with interpreting investment treaties, were mentioned as contributing to a lack of consistency and predictability in outcomes. It was further said that international rules on treaty interpretation and customary international law were not always consistently applied by ad hoc tribunals.

14. It was added that the long-term nature of investment treaties was such that multiple disputes might be expected to arise under them. Therefore, ensuring consistent interpretation of the treaty provisions would enhance the stability of the overall investment framework. It was further mentioned that many treaties contained similar provisions on investment protection (such as fair and equitable treatment, the most favoured nation obligation, the umbrella clause and provisions on compensation for expropriation). It was reported that, in the experience of some States that had

concluded a number of investment treaties with similar provisions, those investment treaties had been interpreted differently by tribunals, including in an instance of concurrent proceedings in which the facts, parties, treaty provisions and applicable arbitration rules were identical.

15. It was said that predictability of treaty interpretation was also critical to allow States to understand whether their actions, such as possible future legislative or regulatory activities, might breach their obligations, and to set their investment policies. Predictability would also allow investors to assess whether certain treatment was in accordance with treaty obligations. It was further said that the existing lack of consistency imposed significant costs because of the consequent lack of predictability, as each party could often point to differing interpretations from other cases in support of its arguments. Interpretation of certain standards in investment treaties by tribunals was further said to be important for States when negotiating their treaties, as many elements of interpretation could be drawn from disputes under different treaties.

16. It was said that other solutions that had been tried, such as seeking to address concerns about consistency through case law analysis, following quasi precedent, and through references in awards to other decisions, had not proved sufficient. Continuing uncertainties in the interpretation of key notions, such as the definition of an investment and whether investments were required to be made in or for the benefit of the host country, were cited in that regard. Consequently, it was suggested that other mechanisms were needed.

17. A different view was that the lack of coherence and consistency was a logical result of the fragmentation of existing underlying investment treaties and that seeking to achieve coherence and consistency might not be feasible nor desirable considering that the underlying investment treaty regime itself was not uniform. In that context, the possible drawbacks of a consistent and coherent regime based on unified standards of protection were mentioned.

18. In that regard, the reasons for the development of a non-uniform regime were highlighted, noting that the investment treaty regime had been developed taking into consideration elements of foreign policy, economic and trade policy as well as development strategies. It was emphasized that each investment treaty was the result of negotiation among States, with particular State interests and needs in mind and, in some cases, taking into account the interests of a particular region.

19. It was said that varied treaty practice with a wide range of differing investor protection standards as well as ISDS provisions were natural results of that process. It was noted that such divergence was a reflection of the different approaches to and peculiarities of investment protection, which were deliberate in nature and should not be overridden in the pursuit of consistency and predictability.

20. With regard to the interpretation of same or similar provisions in different investment treaties, it was recalled that, though not in the context of ISDS, certain international judicial bodies had stated in their decisions that the mere fact that provisions of a treaty were identical or similar to those of another treaty did not necessarily mean that they should be interpreted identically. From this perspective, the different interpretations by ad hoc tribunals could also be considered as not indicating a lack of consistency.

21. It was also argued that a lack of consistency and coherence as well as fragmentation might be perceptions based on anecdotal evidence. For example, different factual situations might lead to different interpretations of the same treaty provision. It was added that there was a need for more experience sharing among States on inconsistent cases and any negative impact. Furthermore, it was stated that experience showed that domestic courts as well as international judicial bodies, permanent in nature, with an appeal mechanism and bound by precedent, had reached inconsistent decisions.

22. During the deliberations, reference was made to articles 31 and 32 of the Vienna Convention on the Law of Treaties, which provided for general and supplementary

rule of interpretation of treaties respectively. It was highlighted that a treaty should be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose. Therefore, it was said that articles 31 and 32 provided a certain latitude to tribunals to interpret the same provisions in a number of investment treaties differently according to the intention of the parties to such treaties.

23. In the context of discussions of the issue of consistency and coherence, several possibilities for States to tackle the issues through provisions in their investment treaties were mentioned. Examples included clarity in substantive protection standards and in procedural provisions, the inclusion of detailed and perhaps mandatory guidance for arbitral tribunals (for example, binding interpretation) and other procedural tools (such as allowing submissions from non-disputing treaty parties). It was added that consistency in States' instructions to their own legal counsel with respect to their submissions would be critical. As a further measure to achieve consistency and coherence the possibility of issuing joint interpretations by treaty parties to be taken into account by the tribunal was mentioned.

24. In response, it was said that the above-mentioned measures might not be sufficient to provide a comprehensive solution for existing (as opposed to future) treaties. It was added that joint interpretations were rarely used in practice, as once treaties had been concluded, treaty parties might find it difficult to agree on the interpretations. It was therefore stated that a systemic solution was needed, to address both lack of consistency and coherence, which might include a system of precedent. Such a system might also promote the accountability of adjudicators. Possible systemic solutions might include an appellate mechanism or a multilateral court. In that context, the example of the Dispute Settlement Body of the World Trade Organization system, which combined an ad hoc panel and a standing appellate body was given.

6. Concluding remarks on coherence and consistency

25. Another view was that desirable consistency in ISDS should be clarified, as divergences in outcomes might be derived from legitimate distinctions, themselves arising from different facts before the tribunals and the arguments presented by counsel, as well as from differences in the underlying treaty provisions. Second, clarity was also needed on the extent to which undesirable inconsistency in ISDS raised concerns.

26. With respect to the first aspect of the question, there was discussion of two types of potential inconsistency, inconsistency in the interpretation of a single treaty, and inconsistency in the interpretation of an identical or similar provision in different treaties. There was broad agreement that inconsistent interpretations of a provision in a single treaty could be a concern.

27. On the second issue, it was pointed out that divergent outcomes did not raise concerns if they were appropriately based on the proper interpretation of the language in those treaties. However, it was noted that differences in treaty language had been exaggerated and that the vast majority of investment treaties contained very similar if not identical language, and examples were provided to the Working Group.

28. It was also stated that rigid adherence to principle of consistency between arbitral decisions could be dangerous in that it could create a jurisprudence constante that was itself inconsistent with the intentions of the parties. A further view was that consistency did not necessarily ensure accuracy.

29. It was said that the more appropriate consideration was whether decisions were correctly interpreting treaties in line with the rules of public international law, rather than whether they were ensuring consistency with decisions by other tribunals. It was added that the goal of consistency should not be to ensure that same or similar provisions were interpreted identically in all circumstances but to ensure that

unjustifiable inconsistencies did not arise. One cause of inconsistency, it was added, was treaty language that was vague or in need of clarification.

30. It was also noted that there had been inconsistent decisions with respect to general rules of customary international law involving the state of necessity/emergency, the law of attribution, and the legal principles regarding damages.

31. It was suggested that inconsistencies in ISDS arose not from legitimate distinctions but rather from the nature of the system itself, and in some cases from the arbitrators.

32. It was also said that efforts of tribunals to react to concerns and to ensure consistency had not proved successful, and that revising all existing treaties would not be a feasible approach.

33. It was said that consistency and coherence in a legal system were in the interests of all stakeholders, and that a dispute settlement mechanism that issued unjustified conflicting decisions would be unpredictable, and that an unpredictable system would lack credibility and legitimacy.

34. In that light, some States suggested that the Working Group might consider, at the appropriate time, potential solutions to include some type of hierarchical system, an appellate body, an investment court, and a mechanism through which tribunals could direct questions to the treaty partners prior to the issuance of awards. Other States questioned whether such a formal structure was necessary and whether it would provide the appropriate remedy.

35. The Working Group recalled that its deliberations at the 34th session on these issues were to be continued at its 35th session.