United Nations A/CN.9/WG.III/WP.176

General Assembly

Distr.: Limited
17 July 2019

Original: English

United Nations Commission on International Trade Law
Working Group III (Investor-State Dispute Settlement Reform)
Thirty-eighth session
Vienna, 14–18 October 2019

Possible reform of Investor-State dispute settlement (ISDS)

Submission from the Government of South Africa

Note by the Secretariat

This note reproduces a submission received on 17 July 2019 from the Government of South Africa in preparation for the thirty-eighth session of Working Group III. The submission is reproduced as an annex to this Note in the form in which it was received.

V.19-07251 (E)

Annex

I. Introduction

1. UNCITRAL Working Group (WG) III has identified four categories of concerns for which ISDS reform is deemed desirable:

- *Concerns pertaining to the lack of consistency, coherence, predictability and correctness of arbitral decisions by ISDS tribunals*: Divergent interpretations of substantive standards, divergent interpretations relating to jurisdiction and admissibility, and procedural inconsistency; Lack of a framework to address multiple proceedings; Limitations in the current mechanisms to address inconsistency and incorrectness of arbitral decisions;[1]
- *Concerns pertaining to arbitrators and decision makers*: Lack or apparent lack of independence and impartiality; Limitations in existing challenge mechanisms; Lack of diversity of decision makers; Qualifications of decision makers;[2]
- *Concerns pertaining to cost and duration of ISDS cases*: Lengthy and costly ISDS proceedings and the lack of a mechanism to address frivolous or unmeritorious cases; Allocation of costs in ISDS; Concerns regarding the availability of security for cost in ISDS; Concerns regarding third-party funding;[3] and
- *Concerns pertaining to Third-party funding*: lack of transparency and regulation and the impact third-party funding has on different aspects of ISDS, for instance increase in frivolous claims, costs of ISDS and security for costs.[4]

2. The Working Group also took into account a number of aspects raised during the discussion of other concerns as it develops its tools for reform, so that all relevant stakeholders will consider the solutions legitimate. These aspects include: consideration of means other than investor-State arbitration to resolve investment disputes, as well as dispute prevention methods;[5] exhaustion of local remedies;[6] participation of local communities affected by the investment dispute to ensure that relevant issues are presented and considered, beyond submissions as third parties;[7] Investor obligations and counterclaims;[8] and in the context of discussing regulatory chill, the potential impact of ISDS on the regulatory policy of States.[9]

II. Agreed process to identify and advance solutions

3. At its 37th session held in New York from 1–5 April 2019, the Working Group agreed on the following:

- Step 1: By July 15, 2019, States and observer organizations should make submissions to the UNCITRAL Secretariat on what other solutions to develop and when such solutions might be addressed;

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[1] United Nations Commission on International Trade Law (UNCITRAL), Report of Working Group III (Investor-State Dispute Settlement Reform) on the Work of its Thirty-Sixth Session (Vienna, 29 October–2 November 2018), paras. 39, 53 and 63.
[2] Ibid., paras. 83, 90, 98 and 106.
[3] Ibid., paras. 122, 123 and 133.
[4] UNCITRAL, Report of Working Group III (Investor-State Dispute Settlement Reform) on the Work of its Thirty-Seventh Session (New York, 1–5 April 2019) (hereinafter "37th Session Report"), para. 25.
[5] Ibid., para. 29.
[6] Ibid., para. 30.
[7] Ibid., paras. 31–33.
[8] Ibid., paras. 34–35.
[9] Ibid., paras. 36–37.

- Step 2: At its next session in October 2019 (14–18 October 2019, tentative), Working Group III will identify which of the solutions to discuss and when, subject to capacity and scheduling;

- Step 3: Working Group III should begin to elaborate and develop potential solutions to be recommended to the Commission.

4. The objective of this submission is to present South Africa's views on possible reform options, taking into account the context of ISDS and its associated problems and the necessary principles on which any successful reform proposals should be based.

III. ISDS in context

5. Foreign investment has been extensively promoted by international economic institutions as a means for development. In this context, development is understood as financial liberalisation, privatisation of public goods and services, deregulation, openness to foreign investment, fiscal discipline and small governance. The meaning of development therefore involves the notion of economic growth through the free market, individual property and free flow of capital.

6. It is often said that the best way of achieving development is through economic growth, and in order to achieve this, the guarantee of a free market and fair competition is needed. Moreover, to achieve development it is necessary to provide as much protection as possible of private property and contractual rights as well as ensure the free movement of global capital through international trade, commerce and foreign direct investment (FDI). The role of the State is seen as that of creating and preserving an institutional framework appropriate for such practices. In this view, the State is responsible for securing property rights to optimize market development. The State's distribution of resources including healthcare, housing, education, water, sanitation, etcetera, is thought best left in the hands of the market – the State should not intervene in this distribution as its interests could affect neutrality and fair competition in the market.

7. In terms of this view, human rights are regarded as an expensive cost of production and people who live in the areas of development projects are regarded as part of a legal risk that needs to be addressed. Local communities are being displaced from their traditional areas in order to clear up the space for investment projects and yet are not provided with new jobs or opportunities and there is little or no consideration for their cultural, social and political attachments to their land. In this logic, the investors' property and contractual rights supersedes public interest and public needs. Added to this, investor rights are protected by several instruments such as international investment agreements (IIAs) and investor-State contracts. Through investment treaties, States guarantee rights to investors, some of which offer similar guarantees to those contained in international human rights law, such as the right not to be arbitrarily deprived of property and the right to equal protection under the law. At the same time, some of these investors' rights can affect issues of public interest such as health, labour conditions, food security, environment and access to safe drinking water.

8. ISDS allows foreign investors to bring claims against host governments to an international arbitral tribunal and gives private parties access to the supranational level. This discriminates against companies operating locally and comes with systemic issues. Yet, people and communities harmed by foreign investments do not have clear mechanisms to claim justice and reparation. Their rights are subject to a system driven by purely private commercial reasoning prompted to award cases exclusively focused towards serving the private economic interest of investors.

9. The fact that the public are not able to participate in the negotiation of investment treaties or in their disputes should be enough of a reason to demand adequate and effective incorporation of human rights law in IIAs. In addition, the fact

that the current international human rights law framework obliges only States to promote, protect and guarantee people's rights ignores the current global economic order in which corporations hold a greater power of influence over people's lives without the need for being accountable for their actions; at least, not by formal means. As a result, countries are faced with an unbalanced system where multinationals receive protection through the ISDS enforcement mechanism, while human rights and the environment are only protected through non-enforceable "soft law". ISDS therefore brings the public interest and the people's rights into the arena of private law.

10. Foreign investment is far from being just an exclusive private issue relating to investors' economic profit. Instead, it involves human rights and public interest concerns. Therefore, interaction between human rights and international investment law raises fundamental concerns. However, investment treaty law provides its own interpretation of how investors' rights must be construed and enforced, diverging in important ways from human rights law. Furthermore, the enforcement of these guarantees for investors can in turn, implicate the human rights guarantees of others who may not be represented in such proceedings.

11. As such, the current international investment regime is detrimental to public budgets, regulations in the public interest, democracy and the rule of law. The current regime does nothing to protect the rights of people affected by foreign investment. There are no binding international obligations for multinationals on human and labour rights as well as environmental protection and affected individuals and communities have no recourse to international justice when multinationals violate their rights. Multinationals, as private profit entities, need to be subjected to the public interest not just at domestic level but also at the international level.

12. Countries need to evaluate the costs and benefits of international investment treaties and reflect on their future objectives and strategies. It is also necessary to include specific language aimed at making it clear that the investment protection and liberalisation objectives of investment treaties must not be pursued at the expense of the protection of health, safety, the environment or the promotion of internationally recognized labour rights.

13. More and more countries are trying to address the ISDS asymmetry by changing or exiting from the international investment regime and are pushing for a binding United Nations Treaty on multinationals with respect to human rights. Such a treaty should include binding obligations for multinationals and an enforcement mechanism, and as such contribute to ending the impunity that multinationals enjoy with respect to human rights violations and ensuring access to justice for people and communities who are affected by multinational abuses. There should be no place for agreements that give multinationals power to sue governments fulfilling socioeconomic needs. Instead, policy space should be safe guarded:

- For promoting and protecting human and labour rights, people's health and the environment;
- To enable countries to transition without facing costly obligations and liability risks;
- For establishing the primacy of human rights and environmental law over profits desires.

IV. Approach to reform

14. Any reform about the international investment regime needs to begin with the very purpose of the regime. Given the origin of IIAs, its principal purpose has been, and remains, to protect foreign investors and, more recently, to facilitate the operations of investors, seeking to encourage in this manner additional FDI flows. However, this purpose alone is no longer sufficient – it needs to be expanded. In

particular, IIAs need to recognise, in addition, the need to promote sustainable development and FDI flows that support this objective.

15. There must be a conscious recognition of the principle of sustainable development through promoting and facilitating investment and ensuring responsible investment. This also means that reforms should be aimed at promoting the development of an inclusive investment related dispute settlement alternative.

16. In addition, ISDS reform must be consistent with broader sustainable development objectives. As Working Group III begins Phase 3 and seeks solutions to the concerns that have been identified, it is important that States' deliberations be guided by their international and national obligations. Any solutions arising from Phase 3 must advance the United Nation's objectives most recently articulated in the Sustainable Development Goals (SDGs). Promoting and attracting investment should not be an end in itself, but a step towards realising the broader objectives of the SGDs and the human rights obligations, such as reducing poverty and hunger, empowerment of indigenous peoples, promoting decent work, and reversing environmental degradation and climate change.

17. ISDS reform discussions must consider an expansive range of reform proposals and allocate sufficient time for their discussion. The reform discussions must also be aimed at promoting a coordinated, comprehensive and inclusive investment-related dispute alternative, one that also speaks to transparency in ISDS and participation of non-disputing third parties that are affected by ISDS proceedings, or participation of public interest organizations in ISDS proceedings to act as advocates for specific global interests.

18. Additionally, there is need for an alternative to ISDS in the form of a more modern and structured dispute settlement process – one that is better adapted to investment disputes that involve sustainable development, public policy issues and a range of different stakeholders and interests.

19. Any discussion on ISDS has to be located in a wider context and reform dialogue – to include reform of the terms of the underlying treaties, because reforming ISDS is in itself not sufficient to solve the current problems the regime faces. Many problems of the current regime can only be tackled through a reform of substantive standards.

20. South Africa is of the view that we cannot divorce the procedural from substantive concerns as they are intricately related. Given that the UNICTRAL process is government-led and the Commission when giving the mandate agreed that broad discretion should be left to the Working Group in discharging its mandate, the Working Group would not be fully discharging its mandate if discussions on the substantive concerns were excluded.

21. Only systemic reform will allow addressing concerns with ISDS in a comprehensive fashion. Piecemeal approaches will only have limited effects as "old" IIAs continue to exist and investors are able to structure their investments to benefit from those treaties.

22. The principle of sustainable development requires understanding investment law not as an obstacle to development but as a tool for host States to achieve their development objectives. At the same time, the principle of sustainable development also demands that foreign investment is subject to effective regulation at both the domestic and the international levels to avoid environmental and social harm.

23. Countries therefore need to undertake systematic, sustainable development-oriented reform. In doing so, countries need to locate IIAs in the wider context of sustainable development and countries need to align national and regional development aspirations. In this context, the role of investment law and any investment dispute settlement system must consist of fostering the political stability needed for domestic and foreign investors to engage in growth-oriented economic activity without hampering the pursuit of competing public concerns.

24. Countries therefore need to move towards agreements that:

- Enable investment for development;
- Ensure investment rules serve economic growth;
- Ensure sustainable development is mainstreamed in investment policy discussions in general and that sustainable development is also factored in the new generation investment treaties;
- Ensure that the objectives of inclusive growth and sustainable development are at the core of national and international investment policies; and
- Ensure that an investment dispute system is undertaken with a view to promoting sustainable development.

25. Countries need to promote and facilitate investment to ensure responsible investment. Domestic companies and multinationals must contribute to sustainable development and decent work by respecting the rule of law and workers' rights through their operations and investments, and by aligning their corporate initiatives with public policies and country decent work priorities.

26. Countries need a broad, pragmatic, balanced, and comprehensive mechanism that takes into account a complexity of cross-border investments and is flexible enough to deal with a variety of disputes involving diverse and potentially conflicting interests, rights and obligations.

27. Countries must aim at solutions that provide adequate protection and preserve regulatory policy space.

28. Despite the growing consensus about the need for ISDS reform, the scope, modalities of, and strategies for that reform remain contested. For systemic ISDS reform to be successful, it is crucial to develop reform proposals that effectively and legitimately address identified concerns and proposals that are based on a normative framework that is globally consented. The framework developed can be used to formulate a number of concrete proposals for investment law reform and the implementation of mechanisms that allow States to ensure that ISDS develops in a manner that is democratic, respectful of human rights, and in line with the rule of law.

V. Principles for reform

Protection of fundamental and human rights

29. Protection of fundamental and human rights is a globally shared constitutional concern that can serve as a yardstick to reform and redesign ISDS. Countries must take into account the importance of human rights in informing international investment relations and in any ISDS reform. This requires that decisions taken by any dispute settlement mechanism must have regard for competing non-investment concerns, and that they do not create obstacles for governments to fall short of fulfilling human rights obligations.

Policy Space to regulate

30. There should be policy space for host States to regulate in the public interest.

Level playing field

31. There must be balanced rights and obligations of host States and investors in the interest of development.

Inclusivity

32. There must be transparency in ISDS and for participation of non-disputing third parties that are affected by ISDS proceedings. This should include participation of public interest organizations to act as advocates for specific global interests that an

ISDS proceeding may involve. The reforms should thus be aimed at promoting the development of an inclusive investment-related dispute settlement alternative.

Respect for the rule of law

33. The rule of law demands coherence and predictability and it calls for structuring ISDS in a way that access to justice does not become prohibitive.

Protection of responsible investment

34. Protection should be limited to claims by responsible investors who have not violated any law, rules, regulations and internationally recognised values, or participated in corrupt activities, and exclude claims that target public interest legislation.

35. To achieve the degree of systemic change that is necessary to meet UNCITRAL's objectives, these procedural reforms to resolution of investment disputes could, and should, be accompanied by significant changes to investor protection rules. These include limiting the definition and scope of investment and most-favoured-nation treatment, and excluding or severely restricting the most controversial mechanisms for challenging States' regulatory decisions, such as indirect expropriation, fair and equitable treatment and physical security beyond standards of customary international law. Corresponding investor-responsibility obligations should also be included.

VI. Possible reform solutions

36. The current international investment law community finds itself at a crossroads concerning the use of appropriate methods for the resolution of international investment disputes. In order to advance discussions on the merits of ISDS, it is necessary to consider whether there are other approaches that might better serve its aims, and at a lesser cost. The focus is thus on finding a balanced, acceptable and workable solution to the investment disputes.

Necessity of Investor-State Dispute Settlement *– Countries must consider whether there is a real need for ISDS mechanisms.*

37. The question is whether ISDS mechanisms are desirable or necessary in the first place. Countries must not rush into assuming that ISDS policies must be a part of their investment agreements and must be mindful of the origins of the ISDS. It was never seen as a substitute for domestic legal dispute settlement, but as a stopgap in cases of extreme maladministration carried out by governments.

Dispute prevention policies – DPPs

38. DPPs are instituted prior to the existence of an investor – State dispute or even a conflict. They help to prevent or efficiently deal with potential investment disputes, reducing the possibility that investment disputes may escalate into an international arbitration. DPPs therefore seek to prevent disputes.

39. DPPs can be considered as a promising approach to addressing the problem of increasing ISDS cases. While ADR processes, like arbitration, still have to deal with an existing dispute that needs to be settled, the prospect of not having a dispute at all must be the preferable option in the view of governments.

Alternative Dispute Resolution – ADR

40. ADR is an alternative to both investment treaty arbitration and resort to national courts. ADR can involve either conciliation or mediation, but it may also concentrate on a fact-finding exercise that makes it possible to narrow down the actual extent of the dispute. The process aims at resolving disputes.

41. The advantage of these alternative approaches is to provide for a faster and less costly settlement, the more so when the problem is tackled at an early stage and with the specific goal of avoiding escalation.

Domestic administrative review procedures *– Administrative review of the law or measure that the investor considers to be in violation of the treaty.*

42. An additional way forward to prevent disputes from escalating is by putting institutional mechanisms in place that allow aggrieved investors to initiate procedures in the host State for undertaking of an administrative review of the law or measure that the investor considers to be in violation of the treaty. Such an administrative review has the advantage that it may allow for an easy fixing of a problem. Such recourse to an institutional or amicable administrative procedure could benefit both the governments and investors involved.

Domestic courts *– Local remedies must be exhausted before access to ISDS.*

43. This would ensure that domestic judicial institutions get a first shot at managing government conduct before a case can proceed to ISDS. This would also align investment law with customary international law and international human rights law, and would help to prevent incompatibility with national laws and regulations.

44. ISDS stymies good governance. By resorting to international arbitration, ISDS substitutes the use of domestic legal institutions and can thereby entrench their weaknesses. The availability of ISDS on the international level relieves States from external pressure to improve domestic government mechanisms and practices.

45. The difference in law for foreign and domestic enterprises is that the availability of ISDS entails is not only procedural, but also substantive challenges. As domestic courts are largely bypassed, arbitration tribunals have powers to interpret and apply issues of domestic law from a commercial rather than public policy perspective, often resulting in a balance tipped in favour of private rather than public interests. Investment arbitrators are generally specialists in international investment law, and are not necessarily familiar with the intricacies of a domestic legal system. In order to be respectful of domestic political communities, there should be a requirement to defer to domestic authorities on matters of domestic law.

46. Even in human rights law, the person who has allegedly suffered a violation must first turn to domestic authorities with his or her grievance, thus allowing them to correct any injustice that may have occurred. Why should foreign investors be immediately entitled to raise their grievances at an international level, without first being required to exhaust domestic remedies?

Ombuds office *– Setting up an ombuds office to serve as a one-stop-shop for complaints.*

47. For investors, an ombuds office provides an official channel to address issues and problems at an early stage. It can constitute a way for the investor to attempt a prompt, early, potentially cheap and amicable resolution of a problem relating to its investment. For host States, an ombuds office constitutes a first contact point or gateway to deal with a problem encountered by a foreign investor. The ombuds office can provide early information to the authorities and enable them to assess the problem. It may also facilitate early action, if required, allowing the authorities to correct the problem before it worsens.

State-State cooperation in dispute prevention *– State-State cooperation rather than confrontation – the interest of having a complaint addressed in a quick and uncomplicated matter is likely to be preferable than costly and time-consuming ISDS procedures.*

48. There are State-State joint commissions set up for cooperation and the purpose of handling complaints of investors and channelling them to the right government agencies for further review. Investors could approach the representative of the joint commission in their home country, who would then engage in respective consultations

with its counterpart in the host State to attempt an early settlement of the emerging dispute.

Arbitration institutions

49. Arbitration institutions also have a role to play in making the resort to alternative means more commonplace within the international investment law community:

- Arbitration institutions could propose simplified rules for ADR or provide for more flexibility in rules on conciliation, mediation and fact-finding, so as to make them more attractive to those wishing to use them in legal proceedings on investment matters;
- Arbitration institutions could also facilitate the access to ADR procedures by developing capacity or encouraging the inclusion of experts on ADR techniques in their lists;
- Arbitration institutions could also further develop their support to parties wishing to go for an ADR procedure – such support could be logistical, secretarial, etcetera.

International organizations (IOs) *– International organizations (IOs) could play an important role in building awareness within the international investment community and among States of the possible advantages that alternative approaches to investment treaty arbitration could bring*.

50. IOs could provide advice on the design, establishment and implementation of adequate policies for dispute prevention and avoidance, including any necessary technical assistance and capacity-building. This will allow States to strengthen their institutional frameworks for the prevention of investment disputes.

Precedent – Precedent is the foundation for consistency and a coherent body of law and should be binding

51. Arbitrators already frequently reference and cite previous investment awards creating a type of de facto persuasive precedent, but this still produces inconsistent decisions as not all arbitrators follow this principle.

Legal standing *– Everyone affected by proceeding to have standing*.

52. Allowing claims by investors against States, but also other affected individuals or communities to bring claims against investors means allowing natural or legal persons with a direct and present interest to intervene in the proceedings. This is a necessary part of making the process fairer and making it a forum that protects the rights of all people – not just those of multinationals.

53. This is different from amicus curiae briefs. The current amicus process has been haphazard and inconsistently applied. Often, the absence of text specific binding provisions to permit intervention has resulted in denial of status. For there to be meaningful public participation, there must be clear textual rules setting out the ability of the public to participate.

54. To ensure that the multilateral investment court (MIC) meets the best practices of an open and transparent process, there must be more clarity on third-party interventions. There is a need to ensure that intervention is done in the public interest and not for unfairly affecting on the parties to the investment dispute. There must be rules that provide a guarantee that the MIC's acceptance of an intervener would assist the Investment Court in determining the issues by providing new or independent views.

Jurisdiction *– Limit jurisdiction to claims by responsible investors who have not violated any law, rules, regulations and internationally recognized values.*

55. Clean hands approach and dismissal of claims associated with violations of any laws, regulations, or international obligations.

Public interest carve-out – *This clause would exclude challenges to public interest laws, regulations and legislation*.

56. Need to ensure that investors are not able to challenge legitimate public interest regulations.

57. A public interest carve-out is important, because one of the most serious downsides to ISDS is that investors have used it to challenge socioeconomic policies and regulations with the threat of litigation.

Supremacy clause – *A supremacy clause clarifying that investment protections do not outweigh countries' social, environmental and human rights commitments*.

58. Countries must have the policy space they require to fulfil their international social and environmental commitments. Including a supremacy clause would make clear to investment arbitrators that obligations arising out of international environmental, social and human rights agreements trump obligations arising out of IIAs. In the event of a conflict between these rules, investor protections would give way to public social and environmental obligations.

Code of Conduct arbitrators – *Develop a Code of Conduct that addresses the ethical conduct of those deciding investment disputes, providing a clearer set of binding rules that guarantee the independence and impartiality of arbitrators, and adopt better rules for arbitrator disqualification*.

59. There is concern that arbitrators on ISDS tribunals do not act in an independent and impartial manner. Because the individuals in question may not only act as arbitrators, but also as lawyers for companies or governments, concerns have been expressed as to potential bias or conflict of interest. Countries are concerned that the system creates conflicts of interest because arbitrators are also lawyers and might expect to get business from the investors in future.

60. A Code of Conduct to prohibit the judges from engaging in legal counsel work on similar cases – double-hatting, and create independence and impartiality obligations. Issues related to term limits and re-appointments must also be included – judges must only be eligible for appointment to one term.

Costs – *Case management procedures, regulate arbitrator fees, cap on arbitrator fees.*

61. Streamlined processes and procedures, prescribed timeframes, and a transparent fee structure will enable efficient and effective case management, thereby reducing costs.

Security for costs provisions – *Security for cost provisions and tribunal to suspend or terminate proceedings if security of costs is not paid within stipulated period*.

62. Security for costs would ensure that countries could enforce awards in their favour on costs of arbitration and legal fees. This is necessary as countries often face the difficulty of enforcing awards granting costs associated with defending ISDS cases. The security posted should be proportionate and reasonable, taking into account a number of factors, such as the amount of the claim. Requirements for security for costs could dissuade claimants from initiating meritless, abusive and frivolous claims. Security for costs should be a mandatory requirement in cases funded by third parties.

Regulatory chill – *Exclusions/Carve outs to ISDS should be introduced*.

63. Often, investors use ISDS strategically, publicly and repeatedly filing cases to coerce governments to agree on favourable terms for their investments, rather than turning to ISDS as a measure of last resort. Even though IIAs do not in themselves directly limit the legislative or regulatory powers of States, they may lead governments to thread more cautiously – and hence potentially insufficiently from a public-interest perspective – when planning and designing regulation. As such, governments might refrain from imposing regulatory measures in the public interest due to the threat of investment arbitration and the high damages it entails.

Counterclaim – *State should be allowed to bring counter claims against investors of breach.*

64. The State is always defendant and cannot bring counter-claims against investors for any breach of their obligations. The system is asymmetrical and should allow counterclaims to address the imbalance in the existing ISDS mechanism.

Investment Insurance – Investment insurance instead of ISDS

65. One proposal is to have recourse to investment insurance instead of ISDS. Political risk insurance – which is available from private and public sector providers – can help protect investors from losses due to legal uncertainty, war and civil strife, expropriation, physical harm, transfer restrictions, breaches of contract, etc.

Unifying language of substantive obligations

66. There must be a unifying of the language of substantive obligations in IIAs to ensure consistency.

Third-Party Funding (TPF) – *Third-party funding should be banned. If not banned, the existence and identity of third-party funders should be disclosed to avoid conflicts of interest, there must also be disclosure of the funding agreement, and must there must be sanctions for non-disclosure agreement. There must be security for costs where there is TPF involved.*

67. There are serious policy reasons against TPF of IIA claims – for instance, it may increase the filing of questionable claims. From a respondent country's perspective, such frivolous claims, even if most of them fail, can take significant resources and may cause reputational damage.

68. Given that most TPFs are profit-driven entities, they have no interest in the substantive issues presented before the arbitral panel. Consequently, they are more likely to invest in claims having the potential for high volume awards. In addition, funders are not parties to the investment arbitration strictly speaking, but by offering financing they gain control and economic power over the claim. They can therefore influence the management of the case and ultimately the outcome of the dispute between the investor and the respondent State. Furthermore, countries, being always the defendant, cannot counter-claim. This means that the TPF always is paid by the respondent host country. Effectively, host countries are the payers of TPF investment arbitration. This is problematic given that such monies are from tax revenue. Therefore, there is a serious risk that TPF will pose a significant burden on host countries and affect regulation.

69. In addition, so much is still unknown about TPF in international investment arbitration and important questions arise with respect to TPF. Is recourse to TPF a necessity or a mere corporate finance decision? Who is really requesting TPF – small investors or big companies? The assertion that TPF does not bring more frivolous claims because of the due diligence and screening process funders go through before financing a claim seems to only partially reflect economic reality. TPFs often form a portfolio of cases, enabling the funder to adopt a more speculative attitude and undertake "risk diversification strategies". There is a very real potential for an increase in the number of international investment arbitration cases that could have a very significant and negative impact on respondent host countries, more specifically developing countries.

Investor obligations – *Investor rights ought to be made conditional on the presence of investor obligations. Without achieving such a balance, investment law will be one sided and undemocratic.*

70. There are many investor obligations that could usefully be added to investment law. Most acutely, there is a need to uphold minimum levels of environmental and labour standards – this would be to provide for investor obligations directly in the treaties, it would contribute to creating an international minimum standard.

Frivolous claims

71. *Dismiss frivolous claims.*

Requirements for information disclosure and security for costs *– Crucial information regarding the nationality of the investor, the existence of a qualifying investment, and the nature and extent of claimed damages can enable states to identify defects in cases justifying early dismissal.*

72. This can enable states to identify defects in cases justifying early dismissal**.**

Damages – Guidance instrument for awarding damages

73. This could reduce inconsistency and unpredictability of awards.

No Reflective loss rule – No reflective loss claims

74. Only loss recovery by directly injured companies should be allowed and not indirect claims – shareholders should be prevented from bringing claims where their loss merely reflects loss suffered by the company they are shareholders of. This ensures that shareholders can only bring action for losses of the company, and cannot allege suffering a loss in a personal capacity for a personal right. This ensures that there is no double recovery. Many indirect claims are associated with abusive practices such as forum shopping and parallel proceedings.

Multiple claims *– Consolidation of multiple claims instituted under same treaty.*

75. The benefits are time and cost saving, and also ensures that one decision is rendered for cases with similar facts.

Statute of limitations

76. Statute of limitations for bringing claims.

MIC & Appellate Body

Both MIC & appellate mechanism could serve the rule of law by introducing an additional instance that could ensure the correctness of decisions rendered in ISDS.

77. However, it is doubtful whether they can also increase coherence in ISDS and contribute to the emergence of a jurisprudence.

78. The MIC has the potential to create an independent and legitimate system for investment treaty dispute settlement, but this can only occur where the process for establishing the court is done in a fair and neutral manner. Compared with ISDS a MIC may bring institutional improvements. Such improvements, however, do not solve the discrimination and systemic issues.

79. The advantage of an appellate mechanism over a permanent investment court would likely be that its creation is politically easier to achieve than the establishment of a MIC. Further, an appellate mechanism could be combined with the existing arbitral system as a first instance. Such a system could draw on the experience in World Trade Organization (WTO) dispute settlement mechanism, where the WTO Appellate Body (AB) oversees a system of panels that are put together for each individual dispute. Compared to a permanent court with tenured judges that would need to be paid independently of the existence of actual cases, such a system is likely more cost efficient.

80. The proposal for an investment court put forward by the EU does not address any of the substantive inequities and imbalances from the terms of the investment treaties. As such, the system of pecuniary awards will continue to provide incentives to investors and law firms to pursue cases that they might not otherwise as the system is based on the many poorly drafted, ambiguous IIAS that allow for expansive interpretations.

81. The extent to which a court can increase consistency in decision-making also depends on the applicable law. If the law remains in bilateral treaties, consistency will be more difficult to achieve, leaving a risk that a court may further expand the scope of investor guarantees in a more permanent way. Therefore, it is doubtful a court would reduce uncertainty in decision-making and increase predictability and legal certainty for both investors and host governments.

82. There are no suggestions that investors would first need to exhaust local remedies or show that domestic courts would be unable to handle a particular case before they gain access to the investment court.

83. Additionally, there are no safeguards that prevent the proposed court from creating regulatory chill. These broad, substantive rights create a risk of financial liability that leads to a chilling effect on decision makers.

84. There is no mention of investor obligations nor legal instruments, which could establish such obligations.

85. There are also no restrictions on investors to access the system, so even investors who have abused their workers or polluted the environment will be able to bring their cases. A court is not going to change this, thereby perpetuating the current problematic ISDS system.

86. How will the MIC interact with domestic courts if assistance from national courts is needed? The MIC should be required to involve domestic courts of the host state for matters of domestic law. This would not only ensure proper guidance on how domestic law should be understood, but also help to avert the risk of the agreement being found incompatible with national laws.

87. An appeal allows the court to modify an outcome. What will the grounds of appeal be? i.e., errors of law or fact – what other grounds will be considered? Will the AB have authority to make its own determination of facts or will all questions of fact be remanded back to the initial tribunal? Will the AB have the authority to order interim and interlocutory relief to preserve the status quo pending the determination of the Appeal? How many judges will it be composed of? The AB would need its own working procedures, including time limits. Its judgments should be published and prior decisions should be given persuasive precedential authority for subsequent cases, providing a framework of legal authority on which to decide disputes brought to the Court.

88. The establishment of an investment court comes with its own problems. An appellate mechanism and a permanent investment court would require setting up as a multilateral institution that is able to oversee ISDS cases independently of the disputing parties and the applicable IIA. For such a system to work it would in practice be necessary to create a multilateral treaty establishing the investment court and defining its competence. In addition, the creation of an investment court would either necessitate the adaptation of bilateral and regional treaties currently offering consent to arbitration, or creation of its own mechanism for submission by States. These huge structural problems would have to be overcome.

89. Introduction of a multilateral court system could also raise its own legitimacy concerns. The selection of judges – who sits as decision makers, and who appoints or elects them? Where would such a court be headquartered and would there be associated privileges and immunities for the institution? The selection process of tribunal members needs to be highly scrutinised given the concern that ISDS arbitrators responsible for expansive interpretations, may reappear as MIC judges and there should be State control over the appointment process rather than giving both investors and States control.

90. The MIC seems to offer the promise of moving away from a model where cases are decided primarily by judges from the specific parties of the dispute to an autonomous judiciary. Mechanisms to appoint judges will be key and the recent controversies over politicisation of appointments to the WTO AB, suggests the

complexity of designing an appointments process that cannot be dominated or manipulated by a State or States determined to politicise it.

91. It is foreseeable that there will only be a few seats for judges. This will result in competition among the different interests from countries in which political power will play an important role to control the court. That power will need to be shaped by clear and transparent rules to avoid inequality and biased judges.

92. Concerns remain about ensuring diversity in the composition of the court and the process for addressing challenges to judges. Best effort should be taken to achieve diversity in the membership of the tribunals – geographic, male/female, etcetera.

93. Judicial independence is an important prerequisite for the credibility and legitimacy of international courts and tribunals. This merits a close review of standards of judicial independence and impartiality, to avoid any kind of bias by possible MIC judges and to ensure their independence.

94. Justice and rule of law are not simply satisfied by the announcement of a new MIC. Given the central importance of enforcement to the overall success of the MIC, the powers such a court will have and whether its decisions will bind and will be enforceable are important considerations for the countries supporting the creation of a MIC. Additionally, would awards made by the MIC be enforceable under the New York Convention or the ICSID Convention?

95. The procedural rules adopted by the MIC are important. The MIC (both First Instance and Appellate Tribunal) will make important decisions governing both private and public rights and obligations. The MIC must have a detailed set of rules of procedure that are transparent. At a minimum, the MIC must meet the following objectives: be neutral, effective, legally predictable and coherent in its dispute settlement system protection and its enforcement. Unbalanced procedural provisions will erode confidence in the neutrality of the MIC and go against due process, fairness and justice.

96. Many concerns that have resulted in the proposal of an MIC are in relation to the need for transparency and public engagement. Clear and direct provisions are required to ensure that meaningful interventions are permitted, to ensure that the rights of the disputing parties to have an orderly and fair hearing is not compromised. Trust in the independence and impartiality of the MIC depend on the transparency of the process by which judges are selected. The selection of judges should be done through a transparent process that involves consideration of the interests of relevant stakeholders. For there to be public confidence in MIC, it is essential for there to be enhanced transparency and public disclosure about challenges made to members of the Investment Court. Public access must be established to preserve confidence and independence.

97. One continuing issue with the current investment arbitral system is that proceedings and awards are often confidential. For example, UNCITRAL Rules require the consent of all the parties before an award or proceeding is made public, and ICSID proceedings are likewise private. However, ICSID publishes the arbitral awards on its website, and many non-ICSID investment arbitral awards come to public view when the award is challenged in either domestic courts or when the State has to account for payment of an arbitral award. However, the remaining problem is that the investment arbitral proceedings are private, even though most investment disputes are effectively public disputes. Investment arbitration deals with international public law – judging the regulatory actions of a sovereign State – and an award against a State would affect that State's citizens as well. Private proceedings and ad hoc awards give limited public understanding of the arbitral procedures and reasoning. A country is accountable to its people, and the legality of a country's regulatory actions is a matter of public concern that should not be confidential. The MIC would have to open its proceedings to third parties and publish its decisions and reasoning. Countries could incorporate the UNCITRAL Rules on Transparency to

disputes, and where countries feel that these do not go far enough, countries can further enhance such rules.

98. Full membership in the court should not be required to experiment with its use. The court should be designed as a forum both for State-to-State and investor-State dispute settlement. Use of the MIC to settle disputes should be voluntary.

99. The proposed MIC has potential to impede intellectual property rights reform. An example is the United States of America pharmaceutical company Eli Lilly that claimed 500 million Canadian dollars in an ISDS arbitration after Canada adjusted its patent law, to ensure better access to medicine. According to Eli Lilly, Canada's patent reform is not compatible with the TRIPS WTO agreement. Investment adjudicators interpreting and deciding on compliance with the TRIPS agreement could change the dynamic of interpretation, as investors have less restraint than States regarding policy and there is a difference between seeing intellectual property rights as innovation stimulants and seeing them as assets.

100. The proposed MIC risks undermining data protection. Foreign investors would be able to use the MIC to challenge data protection enforcement measures introduced for the regulation of cross-border data flows. As such, the MIC risks undermining the protection of personal data.

101. The proposed MIC has potential to impede action on climate change. To respond to climate change, countries need to shift from high-carbon assets into clean energy. This will require a massive change in investment and the adoption of public policies to support and incentivise the right kinds of investment. ISDS can undermine governments in areas closely linked to climate-friendly policies of prevention, mitigation, and adaptation. Public funds should be used to support the shift to clean energy and not to compensate polluters for their lost future revenues when they fail to adapt their business model in a timely and responsible manner.

102. A MIC, in contrast with domestic law systems, would give investors possibilities to claim compensation. This would make government reforms prohibitively expensive, cause regulatory chill, and thus impede crucial measures on climate change. This further undermines countries' ability to reform, and ability to respond to crises, including climate change.

103. Taking into account the issues that are likely to arise, the MIC proposal seems aimed at keeping many of the key features intact, effectively locking in ISDS. Overall, the MIC proposal amounts to cosmetic reforms, not touching on the fundamental problems of the system. Effectively, the MIC seems to preserve and confirm the ISDS system. An investment court would thus exacerbate and entrench this unbalanced and harmful system.

104. We need to have discussions on ISDS reform and its challenges in a constructive manner, and the debate must be structured beyond ISDS and a court system to include other options for dispute settlement (i.e., dispute prevention, State-State; etc.). ISDS reform should be complemented with reforms to address deeper substantive concerns arising from the terms of the investment treaties.

105. Discussions on ISDS reform could accommodate reference to instruments, such as the United Nations binding treaty on business and Human Rights in order to foster sustainable development-oriented policy coherence. Furthermore, there needs to be a consideration of the substantive investment standards found in the investment treaties.

106. Given the appetite in a number of countries to explore various alternatives, it is crucial that the debates about ISDS reform proceed in a well-informed manner and take into account the interests of all stakeholders in a balanced way.

VII. Conclusion

107. South Africa supports in principle discussions on reforming the ISDS regime and building a new mechanism for resolving investment-related disputes. Not

engaging in reform discussions would come with serious drawbacks in that it would not address any of the challenges arising from today's global IIA regime and would keep the countries exposed to risks created by IIAs in their traditional form.

108. South Africa agrees with the need for an alternative to the traditional ISDS in the form of a more modern and structured dispute settlement process – one that is better adapted to investment disputes that involve sustainable development and public policy issues and a range of different stakeholders and interests.

109. Countries must have discussions on ISDS and its challenges in a constructive manner and the debate must be structured beyond ISDS to include other options for dispute settlement (dispute prevention; State-State, etc.); taking into account other instruments, such as the United Nations binding treaty on business and Human Rights in order to foster sustainable development-oriented policy coherence.

110. Additionally, any discussion on dispute settlement would also have to be located in a wider context and dialogue consideration of reform of the terms of the underlying treaties. Any ISDS discussions must also be aimed at promoting the much-needed development of a comprehensive and inclusive investment-related dispute alternative.

111. It is important to note that reforming ISDS is in itself not sufficient to solve all problems that the international investment regime faces. Many problems already identified in earlier phases can only be properly tackled through a reform of substantive standards.

112. ISDS reform should therefore be complemented with reforms to address deeper substantive concerns arising from the terms of the investment treaties it aims to adjudicate and enforce. There needs to be a consideration of the substantive investment standards found in the investment treaties.

113. Likewise, achieving complete coherence will not be possible if many of the thousand IIAs continue to exist. To achieve a better balance, more coherence, and arrive at a generally more legitimate international investment regime, reforming the substance of investment treaties and reconsidering the form in which they are concluded are equally necessary.

114. There is an appetite in a number of countries to explore various alternatives to the traditional ISDS model. Negotiating new treaties that include ISDS runs counter to the decision by some countries to reform or terminate these agreements in order to protect their right to regulate. It is therefore crucial that the debates about ISDS reform proceed in a well-informed manner that takes into account the interests of all stakeholders in a balanced way.