Investor-State Dispute Settlement under review; current challenges, lack of regulation in the EU-MERCOSUR agreement and basis for the EU-UK and UK-MERCOSUR FTAs

Solución de controversias Inversor – Estados bajo revisión; desafíos actuales, la falta de regulación en el Acuerdo UE - MERCOSUR y las bases para los acuerdos de libre comercio entre la UE y el Reino Unido y entre el Reino Unido y el MERCOSUR

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Abstract: Investment treaties aim to protect the rights of foreign investors and provide legal certainty, generally including an Investor-state dispute settlement (ISDS) system. The increase of criticism towards ISDS -which reached its highest point during the EU-US TTIP negotiations- brought up different concerns. As a result, the Investment Court System (ICS) was developed and incorporated for the first time in the CETA between Canada and the EU, and then in other Free-Trade Agreements (FTA) signed by the EU. However, in the EU-MERCOSUR FTA there is no regulation of a dispute settlement mechanism between investors and States parties. Currently, the United Kingdom (UK) is leaving the EU and negotiations of a new deal with the EU are being developed. In the next stages, the UK will most likely reach different agreements with sovereign states and others commercial blocks. In this sense, there is a possibility that a future EU-UK and UK-MERCOSUR agreement will need to consider whether the ISDS or the ICS will be adopted. Also, MERCOSUR will need to analyse which system it will be willing to adopt in the future in case a dispute settlement between investors and States is adopted, and could even explore a system that includes aspects of both the ISDS and the ICS.

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Resumen: Los tratados de inversión tienen por objeto proteger los derechos de los inversores extranjeros y proporcionar seguridad jurídica, incluyendo generalmente un sistema de solución de controversias entre inversores y Estados (ISDS). El aumento de las críticas al ISDS -que alcanzó su punto más alto durante las negociaciones del TTIP entre la UE y los Estados Unidos- trajo consigo diferentes críticas. Como resultado, el Sistema de Corte de Inversiones (ICS) se desarrolló e incorporó por primera vez en el CETA entre Canadá y la UE y luego en otros acuerdos de libre comercio (TLC) firmados por la UE. Sin embargo, en el Acuerdo UE-MERCOSUR no se regula un mecanismo de solución de controversias entre inversores y Estados partes. Actualmente, el Reino Unido está saliendo de la UE y se están llevando a cabo negociaciones de un nuevo acuerdo con la UE y en las próximas etapas el Reino Unido probablemente alcanzará diferentes acuerdos con otros Estados soberanos y bloques comerciales. En este sentido, existe la posibilidad de que en un futuro acuerdo entre el Reino Unido y la UE y entre el Reino Unido y el MERCOSUR se tenga que considerar si se adoptará el ISDS o el ICS. Asimismo, el MERCOSUR deberá considerar qué sistema estará dispuesto a adoptar en el futuro en caso de que se adopte un sistema de solución de controversias entre inversores y Estados en un tratado a firmarse, pudiéndose incluso explorar un sistema que incluya aspectos tanto del ISDS como del ICS.

Keywords: Investment Court System (ISDS), Investment Law, Free-Trade Agreement, Multilateral Investment Court, MERCOSUR.
Palabras clave: Sistema de Corte de Inversiones (ISDS), Ley de Inversiones, Tratado de Libre Comercio, Tribunal Multilateral de Inversiones, MERCOSUR.

1. INTRODUCTION

The existence, negotiation and promotion of investment treaties is one of the most important developments of public international law in the last decades. They became a key part in the promotion of international investments and therefore in the international economy.

The benefits that investment treaties provide are of utmost importance for every country and specially for the international business market. The legal certainty that investment treaties offers are the base of its importance, making host countries more attractive to them.

In this scenario, one of the key elements of investment treaties is the inclusion of an Investor-State Dispute Settlement mechanism (ISDS). ISDS represents the core part of investment protection and are -or were- considered as one of the most essential elements of them. However, over the last decades the ISDS has been in the public eye, as it became one of the most discussed parts of investment treaties.

Opponents to ISDS believe that countries are abandoning part of their jurisdiction when allowing an investment arbitral tribunal to judge
a sovereign State. In addition, the difference of treatment comparing to a national investor -who only has the right to access to a national court- is under discussion.

As a result, different proposals on how to deal with the criticism against ISDS have been developed. In this sense, one of the most innovative and complex one is the Investment Court System (ICS). The ICS was first included in the EU-Canada Comprehensive Economic and Trade Agreement (CETA) and the EU-Vietnam FTA. The ICS as a new mechanism to resolve investment disputes, creates an international investment court system with an appellate mechanism with the idea of creating in the future a Multilateral Investment Court (MIC).

This new paradigm brings a several number of questions, with no clear answers. Those questions relate to the possibility of showing how the ICS will be more beneficial than the ISDS, how the ICS will protect the jurisdictions of member States and mainly, how its inclusion will help to reach the same goals as with the use of ISDS.

In this sense, the EU-MERCOSUR did not include any settlement dispute mechanism between private parties and States, an aspect that shows the different criteria of the parties involved in its negotiations. Notwithstanding, the EU idea of a MIC in the future will probable intend to include MERCOSUR and some aspects will need to be modified.

The above-mentioned situation and the current negotiations of International Investment Agreements or “IIAs” must be addressed to deal with the current EU and United Kingdom (UK) negotiation after BREXIT. In this sense, in case that a treaty is reached, the way to resolve international disputes will need to be addressed and the model to follow will be a fundamental decision.

In addition, -an essential element of our research- is the discussion on how this new system could be considered as a backwardness, taking in consideration that the creation of a formal system was not something which the developers of ISDS wanted to. Considering that a formal Court system is maybe one of the main disadvantages against ISDS. This breakdown period supposes the debate of the base of the investment protection system.

Is the aim of this study to answer which of the investment dispute settlement systems -the ISDS or the ICS- will be the most beneficial for investments and how the legal community could help to improve them, considering a possible approach for new agreements.

The ISDS how it is today, is not able to deal with the criticisms that currently exists. A combination of both systems is not currently under discussion but is an element which needs to be considered. An answer must be reach in view of the importance of investment treaties and how a good system will benefit the entire community.
2. THE ISDS: CHARACTERISTICS, CRITICISM AND POSSIBLE SOLUTIONS

The inclusion of an ISDS mechanism in an investment treaty has become a controversial issue due to the fact of the increasing number of criticism against it. According to the last information provided by the UNCTAD the treaty-based concluded cases were of 674 by May of 2020. From this number 36,5 per cent were decided in favour of states, 29,4 per cent in favour of investors and 20,6 per cent were settled\(^1\).

Defenders and promoters of the ISDS are focusing on the advantages that -in their own opinion- the system and the investment protection itself provides to the economy. Those arguments seem not to be convincing for those thinking about the asymmetry that investment protection provided to international investors comparing with national or domestic ones. That is why the discussion seems to relate to the nature or the core of investment protection. In the past, the idea of dispute settlement provisions was based on the worries regarding domestic protection for international investors, it is said that:

Rules on private investment in international law deal with the treatment of foreign investment in a country. They ensure that foreign investments receive a minimum of protection from the hosting states and formulate rules that establish a balance between the host state’s vested right to expropriate or to legislate, and the foreign investor’s right to their property and to non-discriminatory treatment with respect to domestic investors\(^2\).

The idea of an ISDS system is to provide a mechanism to assure the right of foreign investors. In this sense, the benefits for investors in the ISDS is having a direct right to use arbitration against the host State as per the existence of a consent of arbitration made beforehand in the correspondent investment treaty. Arbitral tribunals are set for the specific case and parties have the right to choose which rule will be applicable to its case. The treaties provide a variety of choices like the International Centre for Settlement of Investment Disputes (ICSID), the Stockholm Chamber of Commerce (SCC) or the Permanent Court of Arbitration (PCA), etc.

Decisions in arbitration proceedings are final and binding and there is no existence of an appeal body. There is a minor possibility of annulment in certain cases which differ depending on the treaty or the arbitration rules. The annulment is an exceptional mechanism to review an arbitral award when there was a violation of the fundamentals rights of any of the parties. As an example, when the arbitral tribunal exceeded its powers, was not duly

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1 UNCTAD. Investment Dispute Settlement Navigator. (Investment Policy Hub, 2018) Available at: <http://investmentpolicyhub.unctad.org/ISDS>
constituted and in general when any aspects of the procedure breached the parties rights or their right to a due process. But, the annulment does not imply the entire revision of the award itself and the possibility for reviewing the merits of the award is restricted.

The non-existence of an appeal body and the possibility of annulment in minor and specific circumstances made the role of arbitrators to be of upmost importance, an aspect also criticised by ISDS opponents. An aspect linked with the existence of concerns about the independence and impartiality of arbitrators, which is another criticism of ISDS.

Why change the ISDS mechanism? Something clear is that the ISDS system has provided the investor of legal certainty, protecting them mainly from arbitrary powers of States. However, an increase number of criticisms against the ISDS has appeared, mainly when discussing the TTIP, the investment agreement between the EU and the US, which current future is uncertain.

Following a study from the UNCTAD, one of the first criticism to ISDS is regarding the legitimacy and transparency of investment disputes, referring that:

In many cases foreign investors have used ISDS claims to challenge measures adopted by States in the public interest (for example: policies to promote social equity, foster environmental protection or protect public health). Questions have been raised whether three individuals, appointed on an ad hoc basis, can be seen by the public at large as having sufficient legitimacy to assess the validity of States’ acts, particularly if the dispute involves sensitive public policy issues.

This aspect is also associated with the idea of discouragements for States to create public-interest regulations against the interest of foreign investors. Likewise, it is linked with the idea of an intromission in the sovereign power of States. The matter of confidentiality in some of the investment disputes is another current concern.

Another discussed aspect refers to the inconsistency and the alleged incoherent of the arbitral awards. This criticism relies on the existence of:

- divergent legal interpretations of identical or similar treaty provisions as well as differences in the assessment of the merits of cases involving the same facts. Inconsistent interpretations have led to uncertainty about the meaning of key treaty obligations and lack of predictability of how they will be applied in future cases.

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4 Ídem.
The before-mentioned aspect is a direct consequence of the existence of different investment tribunals for each case which have their own interpretations of investment treaty provisions. Also due to the fact that arbitral awards are not a mandatory precedent that arbitral tribunals must follow for new awards. Considering this last aspect as a drawback depends on each point of view as for example according to a civil law perspective, the lack of precedent is not seen as a disadvantage.

Also, even the existence of some contradictory awards, at the end tribunals -in general- are likely to follow the criteria of previous awards.

Traditionally, when thinking about arbitration the speed and low cost were considered as important advantages of the system among others. However, this is not always like this and some concerns and criticisms had been developed also on this regard. Therefore, it has been mentioned that:

Actual ISDS practice has put into doubt the oft-quoted notion that arbitration represents a speedy and low-cost method of dispute resolution. On average, costs, including legal fees (which on average amount to approximately 82% of total costs) and tribunal expenses, have exceeded $8 million per party per case. For any country, but especially for poorer ones, this is a significant burden on public finances. Even if the government wins the case, tribunals have mostly refrained from ordering the claimant investor to pay the respondent’s costs. At the same time, high costs are also a concern for investors, especially those with limited resources⁵.

This is also linked with the fact that some states have required the help of funding from third parties in order to deal with the cost of arbitration⁶.

Regarding the above-mentioned criticism a research from the European Federation for Investment Law and Arbitration (EFILA) named: “A response to the criticism against ISDS⁷”, focus on 11 main criticisms against ISDS, mentioning that:

Critics have raised concerns about the pro-investor interpretation of investment treaty provisions and their perceived unpredictability, the alleged lack of transparency of arbitral proceedings, the alleged lack of independence and impartiality of arbitrators. Others have suggested that ISDS bypasses the operation of domestic law and national courts and stymies the right of states to regulate. Criticisms have also been raised against the investor-state arbitration process itself, claiming

⁶ Is the case of Uruguay that was financed by a TPF in the investment case initiated by Phillip Morris. *Phillip Morris vs. Uruguay ICSID N." ARB/10/7)*
⁷ EFILA (European Federation for Investment Law and Arbitration). A response to the criticism against ISDS. 17/5/2015. Available at: <https://efila.org/2015/05/17/efila-publishes-response-to-the-criticism-against-isds/>
that it allows partisan, self interested arbitrators to secretly overrule governments with no right of appeal.

Numerous interesting aspects come from the report, for example, it showed that generally the majority of cases are won by states and not investors, as mentioned before. In addition, when considering the lack of transparency, the report shows that:

the majority of arbitral proceedings take place under ICSID rules and the ICSID awards have been published on the ICSID website for several years and the new UNCITRAL Transparency Rules introduce the same level of transparency for UNCITRAL proceedings.

Also, the report focuses on the mechanism that arbitration systems nowadays have as to tackle the problems of independence and impartiality of arbitrators, which as referred is also criticised. Connected with the topic of interpretation, the creation of appeal facilities is also considered. The EFILA report mentions that even critics:

recommend that the ISDS system should be reformed and that there should be an appeal mechanism system to ensure that states remain masters of their treaties or that states should be able to issue a binding interpretation of provisions of the treaties. This conclusion not only fails to recognise that international courts and tribunals, such as the International Court of Justice itself, often rely on their past decisions. It also fails to recognise the fact that the State parties when creating the ISDS system have already established a necessary system of checks and balances in order to protect them from the creative interpretation of arbitral tribunals.

Another criticism stated is related with the ‘regulatory chill’. This aspect has been largely discussed internationally as an effect that investment protection will have on States, basically preventing them from passing new law to avoid new claims. The EFILA report mentions that there is no evidence to base this argument and this idea could be confronted with several examples as Uruguay regarding the Tobacco Regulation and the Philip Morris case.

Two more crucial elements are presented by the EFILA report. The first one is regarding the criticisms about the need of investment provisions when negotiating between developed countries or economies, like EU-US, Canada-EU and possibly the EU-UK, which are countries or regions that are considered to have developed a clear ‘Rule of law legal systems’. EFILA mentions about

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8 Ídem.
9 Ibíd. p.4.
10 Ibíd. p.11.
this that: “countries that enact laws and regulations with due process and that respect the rule of law have nothing to fear from international arbitration as their acts are not likely to be challenged”11.

The truth is that a clear developed rule of law does not guarantee that domestic law will be suitable for investors and that they will protect and attract them. A clear example of this is what happened in the Loewen v. USA12, which involved two developed economies, where the domestic remedies could not have been considered as the most suitable to protect the rights of the Canadian investors. Thus, the EFILA opinion about the existence of no evidence seems to be the most accurate one.

Additionally, another criticism developed in the EFILA report is about the relation of investment protection and the attraction of new investors. The case of Brazil and others developing economies is normally used by those who think that; “there is no positive correlation between FDI flows and investment treaties”13. Regarding this, EFILA mentions that “the truth is that investment treaties are one instrument of many which States use to attract FDI”14. And this element is of highest importance, as there are many ways to attract FDI and some of them are more effective than others, but this cannot be an element to ignore the relevance of investment protection. Finally, the EFILA report considers about the ‘elite of arbitrators’ in charge of the decision regarding investment dispute. Stating on this topic that:

investment arbitration is based on a system of party autonomy in which designating parties appoint their own arbitrators. In doing so both parties choose individuals they believe are likely to be sympathetic to their cause. If States indeed feel so uncomfortable with the current pool of arbitrators, they are totally free to expand that pool by selecting “new” individuals15.

Of course, parties are more willing to choose arbitrators which are more credible or who are more prestigious in the academia or investment forum. Nevertheless, this do not suppose there will be more willing to issue an award in favour of investors.

The EFILA report is an example of many studies regarding the ISDS criticisms. An essential element after discussing all the criticism is linked with the fact that many of the criticism relate to the nature of investment protection itself. In this sense, the ICS even try to solve many of its problems, the basis of the ISDS as a system seems not to be changed.

12 Loewen Group. Inc. and Raymond L. Loewen v. United States of America, ICSID Case No. ARB(AF)/98/3.
14 Ídem.
There is a view which consider\textsuperscript{16} that the reform of ISDS needs to be directed by constitutional principles, what implies: “breaking with the prevailing private law thinking in many quarters of ISDS practice”\textsuperscript{17}, what seems to be a change of paradigm. From that point of view, the creation of an appellate body as well as a permanent court is understood to be in compliance with constitutional principles. Considering also that both elements: “would serve the rule of law by introducing an additional instance that could ensure the correctness of decisions rendered in ISDS”\textsuperscript{18} Among solutions provided by the UNCTAD, the introduction of appeals facility and the creation of a standing international investment court is also included.

3. THE ICS AS A NEW SYSTEM

The ICS is presented as the solution to the criticism that currently exists to ISDS with the same aim of resolving investment disputes. However, the system presents some differences clearly visible at first sight. Among this, the existence of a permanent court eliminates the possibilities of deciding without restrictions who will be the judges or the arbitrators that will be in charge of the decision. The incorporation of an appellate body in the ICS represents an important change. Those elements, brings to the discussion an important question, is the new system better than the last one? Unfortunately, the answer is not an easy one.

When negotiating the CETA a traditional ISDS system was included in the investment chapter. However, as a result of the criticism against ISDS which resulted from the negotiation of the TTIP between the EU and US -where the investment chapter was in the centre of the discussion-, different studies advise that the investment settlement provisions of the CETA needs to be redefined. On this regard, it was a public consultation regarding this matter followed by the EU Commission, where they stated that:

The public consultation launched by the Commission on investment protection in the EU- USA negotiations for a TTIP confirmed the desire of sections of EU civil society for further reform of international investment provisions. The replies to the consultation indicated either concern or opposition to the use of ISDS in TTIP and provided comments on the EU’s approach within TTIP\textsuperscript{19}.

Of course, this supposed an alert to the EU in the continuity of the


\textsuperscript{17} Ídem.

\textsuperscript{18} Ídem.

CETA as it was first developed. In this regard, when considering the TTIP the EU Parliament voted a request which considered the replacement of ISDS with a new system\textsuperscript{20}. The decision of creating a “special” and unique tribunal for CETA disputes and an ICS in general represents mayor costs and this needs to be considered, mainly when the cost of procedure was a critic under ISDS. In this regard, the European Union Parliament Research Service (EPRS) mentions that:

The ICS was inspired by the World Trade Organization Appellate Body, both for the selection and remuneration of judges. Judges will receive a retainer fee that may be turned into a salary if workload justifies it, as in the WTO framework. The main reason for the retainer system is the relatively low annual average of cases brought under investment agreements. For example, the North American Free Trade Agreement (NAFTA) and the Energy Charter Treaty, two of the treaties with the largest total number of investor-state disputes, averaged respectively 2.7 and 6.6 cases per year. Because of the low number of cases and to contain the cost of establishing an ICS, CETA uses the International Centre for Settlement of Investment Disputes (ICSID) as an administrative secretariat, charged with providing organisational and logistical assistance for the ICS proceedings\textsuperscript{21}.

In this sense, as to avoid the existence of major costs and with the aim of having the support and logistic assistance of an experience institution article 8.27.16 of the CETA provides that; “The ICSID Secretariat shall act as Secretariat for the Tribunal and provide it with appropriate support.” Naturally, as mentioned, the use of ICSID as an administrative secretariat supposes the reduction of costs that the new ICS will bring. Also, it is said that: “the choice of ICSID for CETA could be related to its current role in NAFTA, but also to the fact that it is currently the main forum for ISDS globally”\textsuperscript{22}.

It is also important to mention that according with Article 8.23.2 of the CETA, the submission of claims to the tribunal could be acquiesced under the ICSID and UNCITRAL Rules. In this sense, and considering the new aspects introduced by the ICS, the report mentions that:

The change to an ICS has been welcomed by some parties previously critical of arbitration, but which were open to reform. However, some of the acclaimed system innovations will be decided only after the establishment of the court (such as the code of conduct), and developments will therefore be monitored. For those supporting arbitration, the switch to an ICS represents a compromise, as it

\textsuperscript{20} EU Parliament Resolution of 8/7/2015.
\textsuperscript{22} Ídem.
maintains the international investment law dispute settlement framework, although the investor has no say in selecting the tribunal members, as it did under arbitration\textsuperscript{23}.

Of course, this element brings criticism regarding on how far the new system is from the former one. However, the approach seems reasonable, mainly when thinking that the aim of both systems is the same.

In September 2015, the submission of the ICS as a new system was made and the EU resolved the inclusion of the ICS for the TTIP but also to other treaties under negotiations as the CETA, this also was approved by Canada. Thus, considering the opinion of the EU, the route for a possible investment treaty between the EU-UK does not seem to be different and seems to be a feasible way for a possible UK-MERCOSUR agreement.

Important is to mention that is in the core of investment law to establish the mechanism to protect investors rights and make the conditions in the host country more attractive to foreign investments. Investors are generally reluctant to be bound by domestic courts, for these reasons it has been mentioned that: “alternative methods have been created for the settlement of disputes between states and foreign investors. They consist primarily of granting the foreign investor direct access to arbitration with the host state”\textsuperscript{24}. Something that is proposed to change with the ICS.

Undoubtedly, the ICS is a new form of settlement mechanism, different from the former one, but designed for international investments. As the EPRS mentions “the main opposition to the ICS comes from those who primarily favoured a domestic approach to such disputes”\textsuperscript{25}. On the contrary, this could not mean that people which support arbitration in investment will probably support this new system.

The new ICS tribunal in the CETA includes a first instance court with a 15 judges list to be selected and an appeal body. Those are the main difference with the ISDS. An investment arbitration nowadays will be dealt by an arbitral court and its decision will be final and biding. As a difference, we not that a first term award under CETA could be revised by the appeal body. Each court will be integrated by three judges or a sole arbitrator, they will be chosen by the President of the tribunal among the members previously appointed. The important aspect is that they must always be from the 15 members previously listed and there is no possibility for the parties to introduce another individual.

There are other essential elements from the CETA to consider, for example the start of each dispute will be with a consultation phase to avoid the existence of disputes and try to solve them beforehand. The effectiveness

of this phase will prevent parties to continue proceedings and therefore reduce costs.

Furthermore, some aspects have been developed to avoid the cases under CETA become expensive. In this sense, being an appointed judge in the CETA is not considered to be a permanent job and they established a system retainer fee with the possibility of creating a salary position if necessary. This is something to consider also when thinking about the possibility of creating a Multilateral Investment Court. As could be seen, the negotiation of the CETA has specifically address the matter of high costs involving court proceedings as to avoid the criticism made to ISDS on this regard. However, in cases involving many jurisdictions and parties from different countries, the problems of cost and fees is difficult to address.

Finally, the ICS included at the CETA seems to be a feasible model to be adopted in a future EU-UK FTA and a UK-MERCOSUR agreement, the EU also included its ICS in the EU-Vietnam FTA\(^\text{26}\). The non-existence of an investor-State dispute resolution mechanism in the EU-MERCOSUR makes the inclusion of an ICS an aspect to be considered in the future.

The ICS appears to be the dispute resolution model to be adopted by the EU in all its future investments treaties. Moreover, it is important to mention that the UK is and was part of the EU when development the ICS so it is probable that would be willing to adopt this system, in for example a UK-MERCOSUR, even this fact is not guarantee.

Notwithstanding, the inclusion of ICS was not unanimously supported at the beginning. In this regard, Belgium ask to the EU Court of Justice (CJEU) to review the compatibility of the ICS with the EU law system. This was a condition of the Walloon regional government to agree on the inclusion of the ICS in the CETA and to ratified it. This is important considering that according to the CJEU opinion\(^\text{27}\) dispute settlement mechanism must be approved by the EU and each member states as it is a share competence.

3.1. The creation of the Multilateral Investment Court

One of the objectives of the CETA through the ICS is the creation in the future of the Multilateral Investment Court (MIC). The EU appears to be determined to create the MIC in the future and the inclusion of MERCOSUR in a possible future treaty is an aspect to be considered.

This is not the first time that the international community aims to develop a kind of MIC. Between 1995-1998, the Organization for Economic Cooperation and Development (OECD) started negotiations to develop a “Multilateral Agreement on Investment” from NGOs. It is argued that\(^\text{28}\) the


\(^{27}\) EU COURT OF JUSTICE. “Opinion 2/15 of The Court” (Info Curia, 16 May 2017).

main difference between the OECD project and the EU proposal is that the first one was more focus on substantive investment protection and the new one is more focus on the procedural side of the investment protection system.

To pursue it goals, the CETA establish as an obligation to follow different steps to create the MIC. Article 8.29 of the CETA provided that the CETA Joint Committee have the power to replace the ICS for the MIC. In the same line, Art. 8.15 of the EU- Vietnam FTA includes an agreement of the parties for the development of a MIC with the same effect as the CETA, adopting also the idea for a multilateral appellate mechanism.

The above-mentioned provisions in part recognised that the ICS is not the best solution, even considered as a previous step for the MIC. However, is the MIC possible or represent and improvement compared with the ISDS? This is a question with a difficult answer considering the current situation of investment law. The MIC seems to be hard to be reached as appears not to consider the current problems that the ISDS have to deal with.

The EU has an important commitment in the pursuit of a MIC. As a result, on 13 September 2017, the EU Commission published recommendations to the EU Council in order to start negotiations for an international agreement including a MIC. Consequently, on 20 March 2018, the EU Council approved, and published negotiating directives were authorised the EU Commission to start the negotiation for a future MIC. In addition to this, in the end of the 2017 discussions on this regard were sponsored by UNCITRAL. After that, on 18 January 2019, the EU submitted its proposal to the UNCITRAL. The last sessions of the working group took place in Vienna on October 2019 and January 2020.

3.2. Criticisms about the new ICS

The creation and development of the ICS is not peaceful and has also brought some criticism. The ICS is not seen as a solution by all members of the civil society, who did not understand the new system as an answer to the current problems and who do not think the protection of investors must be different than the one provided to national ones. The supporters of these
opinions are against not only to the new system but also they seems to be against investment law and its main purpose.

In addition, discussions about how the new ICS will violate the principle of autonomy of the EU legal order has been brought. This relates to the fact of how compatibilized is the system of the new ICS with the EU law. Even this is a specific problem of the EU and not of the system itself, this will be discussed in cases like the CETA and in a possible future agreement with the UK and an agreement with MERCOSUR.

The EU see the ICS as a previous step for the development of the MIC. However, it is not sure that even the ICS or the MIC, will solve the current criticism of the ISDS. Moreover, how the new system substantially changes the older one is over discussion.

For these reasons, the ICS has also been criticised and characterised in a report like the: “... wolf in sheep’s clothing”, alleging to be the “EU’s great corporate privilege rebrand”\(^31\). The same report also refers to the ICS as the Trojan horse of the EU Commission stating that:

> with the exception of some procedural improvements -an enhanced selection process for arbitrators, stronger ethics rules, and the establishment of an appellate body- the re-branded version essentially contains the same investor privileges as existing trade and investment agreements\(^32\).

Adding that the new dispute settlement is not judicially independent based on the fact that:

only investors can sue and arbitrators are paid per case, there is an incentive for the arbitrators (misleadingly re-labelled ‘judges’ in the EU proposal) to side with them as this will bring more lawsuits, fees, and prestige in the future. Restrictive selection criteria, the lack of cooling off periods and loopholes in the proposed ethics code for the arbitrators also give rise to concerns that tribunals will be staffed with the same private lawyers who have until now driven the boom in investment arbitration and grown their own business – by encouraging investors to sue and by interpreting investment law expansively to encourage more claims\(^33\).


\(^{32}\) Idem.

the arrival of the ICS, as they see this new system as a “re-labelling” of the previous one. Even the ICS seems not to be the solution to all of the problems that exists in the ISDS, this position is not shareable as do not consider that the ICS has not been already proved. There is an effort of the EU to bring solutions that must be measured. However, not even the EU knows if this new system will be a successful one.

3.3. The ICS as a solution of the problems present in the ISDS

The ICS is presented by its developers as the best way to solve the problems that the ISDS presents. But, is this a realistic approach? It seems that the new proposal is mainly based on the opinion of the civil society and state countries, but what investors think about a reform appears to be continuously forgotten. In this sense, it is mentioned that:

Making proposals for ISDS reform requires taking stock of the status quo. From the perspective of foreign investors, investment treaty arbitration, which is offered in addition to, or as an alternative for, the host state’s domestic courts, has been successful in making host states comply with their IIA obligations in an effective, neutral, and independent forum for the settlement of investment disputes34.

And of course, how investors see the new proposal is a vital element to consider a reform because investments are undoubtedly needed. Though, sometimes investors -which are key actors- looks to be forgotten. After the existing and development of a mechanism as arbitration through ISDS, the ICS could be seen as a legal setback in investment protection. In this sense, the creation of a permanent body when organizations as the ICSID play a key role in arbitration could be seen as an increasing of costs and as a non-realistic approach.

The appeal mechanism seems to make process longer than the ones where ISDS was involved. One aspect of arbitration -that is seen as an advantage- is that their awards are final and binding. However, the possibility of the annulment is specifically regulated in some cases, and an appeal mechanism looks not to be completely necessary.

The creation of a MIC must be carefully addressed. There is no base to consider that this will signify an improvement in the current system. In addition, the low possibilities of an agreement in the international community regarding the creation of a MIC makes this a phase difficult to be reached.

Naturally, the change and improvement of the ISDS or investment protection will not be automatic and is a process which requires time and patience from all the parties involved. Though, the current conditions entail the need of dealing with the problem urgently.

Regarding this new mechanism and considering the previous criticism,

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EFILA\textsuperscript{35} also addressed this topic. Considering that the ICS is a:

first and foremost, a bold move to appease the EP and the public opinion in many EU Member States, which are critical against TTIP generally, and in particular against including any type of ISDS. The ICS proposal attempts to make the inclusion of an investor-state dispute settlement mechanism in TTIP politically acceptable, while at the same time trying to address the perceived shortcomings of the existing ISDS\textsuperscript{36}.

Aspects that must be analysed in order to accept the ICS as a valid mechanism of protection of States and investors.

4. A POSSIBLE EU-UK FTA AND THE SYSTEM TO BE ADOPTED

As mentioned before, the CETA was the first to add an ICS. Thus, will a possible EU-UK FTA include an ICS? This is difficult to conclude in this primary stage when there is a situation of uncertainty regarding the future of the EU - UK relations but is a possibility that needs to be explored.

When discussing the options for trade for the UK and the EU after BREXIT many options are on the table\textsuperscript{37}. Among them, it is found; (i) Membership to the EEA (European Economic Area); (ii) Become part of the EU’s custom union; (iii) Agreed an FTAs with the EU. A decision that needs to be reached in this transition period after the “exit” of the UK from the EU, the last 31th of January 2020.

Notwithstanding, from the list mentioned above, the negotiation of an FTA seems to be the most beneficial one for both parties. An important aspect relies on the fact that the EU will probably support the use of an ICS as a settlement mechanism if an investment chapter is included in a possible FTA. This is based on the context of the previous TTIP negotiations and the final adoption of the ICS in the CETA. If the UK do not agree with this aspect, new elements will be probably bring to the discussion. Maybe, as happens when you have to resolve problems between cousins, an eclectic approach is reached an aspect that in our view may be the most recommendable approach.

Of course, in the negotiation of the treaty the investment protection aspects will be particularly addressed. As it is regulated in the Lisbon treaty the development of the investment policy of the EU is led by the EU Commission, but it is currently under discussion if the EU commission is able to agree on the settlement dispute system as it affects the sovereignty of EU members.

\textsuperscript{35} LAVRANOS, Nikos et al. “TASK FORCE PAPER regarding the proposed International Court System (ICS)”. EFILA. 1-2-2016.. Available at: <https://efila.org/wp-content/uploads/2016/02/EFILA_TASK_FORCE_onICS_proposal_1-2-2016.pdf>

\textsuperscript{36} Idem.

Is for this reason that these agreements are considered “mixed agreements” defined as agreements which to be approved need the ratification of the EU and also its members.

The CETA was qualified as a mixed agreement by the EU Commission -mainly because of its investment chapter-, thus currently there is no doubt about its legal nature, even this aspect was highly discussed. Therefore, the CETA needs the approval of the EU and each of its member before coming into force. The same will happen with a possible agreement between the EU and the UK if containing and ISDS or most probable a ICS as expressed.

Independent from the form to be adopted, the correspondent agreement will probably have an investment chapter as the protection of investment is a priority for both parties. A chapter that will include a dispute resolution mechanism. A mechanism adopted in accordance with the aim of creating an investment protection system that could be resume in a depoliticised mechanism, which protect investors from any change in domestic law in the aim of bringing legal certainty to them.

Something that the UK must also consider is their approach to the creation of the MIC. After BREXIT, there is a feeling that the UK not seems to be a country open to this kind of agreement or structure involving a foreign Court. Even though, the EU after its commitment in the promotion of the CETA seems to be willing to adopt this kind of provision and also the UK to follow this model. However, this must not be seen as an element to be part in the core of the investment negotiations between the two parties as per the possible UK negative approach to it.

5. THE APPROACH OF MERCOSUR TO THE ICS AND NEW TRENDS ON INVESTMENT PROTECTION

5.1. The EU-MERCOSUR FTA

Last year, the FTA between the EU and MERCOSUR was announced after more than twenty years of negotiations. The future of the agreement is promising. However, the agreement still needs to be approved by all the parliaments of the members of each block. Nevertheless, the text did not include any dispute settlement mechanism between investors and States parties. Additionally, an important aspect to consider is that many EU and MERCOSUR States have IIAs (including ISDS) yet into force.

The inclusion of an investor-state dispute mechanism in the EU-MERCOSUR FTA was a desirable aspect in a treaty of this kind. Nevertheless, only a dispute settlement mechanism between State parties or the blocks as a whole was included. Many reasons could be the ones that reached to the no inclusion of an investors settlement dispute mechanism and they seems to be related with the success of the agreement and its ratification by its members.

Among the reasons, the negative approach of Brazil to IIAs, the concerns about human rights disputes in the MERCOSUR region, the current
situation of the EU regarding intra EU investment and what happened in the CETA negotiations has been reached. Undoubtedly, the criticism against ISDS also had a strong influence on the negotiations results. There is a need to find an attractive mechanism to all parties involved. In this sense, the possibility of creating a system which combines elements from the ISDS and new aspects of the ICS, mainly the incorporation of an appellate body is in our opinion a feasible approach to follow. Also, the need to establish a new system that could deal not only with the general criticism but also with the concern of countries that are reluctant to adopt a dispute settlement mechanism between investors and States, as is the case of Brazil, for example.

It must be considered that the possibility of a renegotiation in the future were the ICS could be included also exists. In our view, the creation of a system suitable to the interest of the EU and MERCOSUR considering the lessons learnt from the future application of the CETA and its ICS mechanism is a possibility to explore. The possibility of creating a system which includes aspects of the ISDS and the ICS and considers legal developments of our region, will represent an effective and acceptable mechanism of solving investment disputes between investor from the EU and MERCOSUR.

In our view, considering that EU and some MERCOSUR States have IIAs (including ISDS) yet into force, it will be the time to replace them by the creation of a unique dispute settlement mechanism between investors and States with clear rules applicable to the countries of both blocks. In this sense, the arguments developed in the EU that rejects the existence of intra-EU BITs are also applicable to this situation.

Finally, in our view, a possible renegotiation will need to includes the correspondent provisions that encompass the EU ambition of creating a MIC. Bringing to the system a Latin American approach that will assure the success of the MIC implementation worldwide.

5.2. The UK-MERCOSUR FTA; an approach to its negotiation

After leaving the EU on 31th of January 2020 it’s time for the UK to look for new FTAs and investment agreement all over the world. This represents a great opportunity to the MERCOSUR in starting a new relation with an important economy like the British one. In this sense, even a negotiation of a deal is far from being reached, it is probable that a possible deal will include an investment protection chapter.

If a FTA is reached, it will be the time for all the parties involved to consider the inclusion and negotiations of a dispute settlement mechanism to solve the investor-State disputes. It is recommendable that this mechanism includes an ICS or an innovative mechanism that considers some aspects.

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38 BAS, Magdalena , Acuerdo Mercosur-Unión Europea: Sombras y Ausencia de la solución de controversias inversor-Estado, DT (2019), Available at: <https://www.fundacioncarolina.es/dt_fc_21/>
form the ISDS and the ICS combined. As the EU will not be involved in this negotiation and considering that the approach to the matter from the MERCOSUR countries and the UK could be different to the one developed by the EU, the system to be adopted needs to crystallize a mechanism in which all the countries involved feel comfortable. Mainly considering, for example, the approach of Brazil that is different from the approach of the others MERCOSUR countries.

It is important to establish that currently Argentina, Paraguay and Uruguay have IIAs with the United Kingdom into force, all including an ISDS system representing an important start for a negotiation of a deal that includes the whole MERCOSUR. In the case of Brazil, the IIAs with the UK was never ratified it⁴⁰. We are not considering Venezuela as it is currently suspended in its rights and obligations as a MERCOSUR member. Nevertheless, the negotiation of a new FTA must consider a new and comprehensive approach of all the parties involved.

The question if an ICS mechanism with a possible MIC in the future would be included and even the existence of a FTA is still uncertain. Mainly considering the Brazilian traditional reluctancy to IIAs and the low probability of the UK allowing a foreign MIC to decide their investment disputes. Of course, the approach of the UK to the CETA was an open one but this was as a member of the EU a condition that has now change. Though, the discussions that currently exists will allow the parties to consider the adoption of a model that complies with their expectations and guarantee investors and States the protection they required. Thus, all the elements presented by the defenders of the ICS and the critics to the ISDS and the ICS must be considered in a future negotiation, that will include the approach of the UK and MERCOSUR countries involved.

CONCLUSIONS

The aim of this article is to answer which of the investment dispute settlement systems -ISDS or ICS- will be the most beneficial for investments and how the legal international community could help to improve both of them, considered as a possible approach for their inclusion in the EU-UK FTA after BREXIT, in a future renegotiation of a EU-MERCOSUR agreement and a possible UK-MERCOSUR FTA. After considering most of the factors that influence on the present topic, a general statement on this matter is far from being clear.

The presence of several criticisms to the ISDS system made the EU and several parties involved to create a new system -the ICS- to deal with the existing criticism. Even the efforts, at a first sight the new system does not seem to be able to cope with them. The inclusion of an appeal mechanism and a permanent Court looks to be a positive change. However, there is no evidence that both represents a unique and effective solution to the criticism.

of the ISDS. Also, the creation of a MIC appears as a difficult objective to be acquired. Additionally, the idea of eliminating arbitration through an ISDS i could result in a setback in investment law instead of an improvement.

Different criticisms and its proposed solutions are forgetting the role and opinions of investors who play a key part in the promotion of investments. The solution cannot rely only on what States and civil society cares about because of the complexity of the problem. In this sense, the adoption in the future of a system that considers the positive aspects of the ISDS and the constructive developments created by the ICS, mainly the existence of an appellate body, seems to be the most prudent approach to this issue. It would be important to analyse how the ICS works as to consider the possibility of coordinating the efforts of the EU in the creation of a MIC.

As a result of this, the best trade deal between the EU and the UK will be the one which includes an investment chapter and assure the promotion of investment. Both are allies and share a common past and must be focussed on their shared future. As the ICS was developed in the EU when the UK was still a member, it is probable that an approach similar to the ICS will be adopted. However, considering the approach of the UK to foreign Courts the possibility of refusing the existence of an ICS and mainly the future creation of a MIC is an element to be considered. Once again, an approach that combines element of the ISDS and the ICS could be the best way to protect investors and promote investment as well.

In the case of MERCOSUR, the inclusion of an ICS in a future renegotiation with the EU must be taking into account by the actors involved. Also, the ICS inclusion in a future negotiation with the UK is a plausible element that needs to consider all the elements presented in this article. Additionally, the creation of a system that includes the advantages of the ISDS and the benefits introduced by the ICS -mainly with the inclusion of an appellate mechanism- and reflects the Latina American approach to investment protection, is in our view the most reasonable step to follow. In this sense, from a MERCOSUR perspective, the approach of Brazil to IIAs for example will be an important element in the discussion. Also, the future of the existence of IIAs between MERCOSUR and EU countries and its future is an aspect to be redefined.

The improvement of the ISDS without changing for the ICS could also be an attractive solution, adopting new and positive elements from the ICS, mainly the existence of an appellate body. Undoubtedly, the work together of all the parties involved will create the best solution, with the possibility of reaching the best system possible and continue improving investment law, investments and its protection.

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Investor-State Dispute Settlement under review. Santiago Theoduloz Duarte


Resolução de litígios entre investidores e Estados em análise; desafios atuais, o acordo UE-MERCOSUL falta de regulamentação e base para os Acordo de livre comércio UE-Reino Unido e Reino Unido-MERCOSUL

Resumo: Os tratados de investimento visam proteger os direitos dos investidores estrangeiros e proporcionar segurança jurídica, geralmente incluindo um sistema de resolução de disputas entre Investidores e Estado (ISDS). O aumento das críticas ao ISDS - que atingiu o seu ponto mais alto durante as negociações UE-EUA TTIP - trouxe preocupações diferentes. Em consequência, o Sistema de Tribunal de Investimento (ICS) foi desenvolvido e incorporado pela primeira vez no CETA entre a Canadá e a UE e depois noutros acordos de comercio livre (ACL) assinados pela UE. No entanto, no TLC UE-Mercosul não existe regulamentação de um mecanismo de resolução de disputas entre investidores e Estados partes. Atualmente, o Reino Unido está a abandonar a UE e estão a decorrer negociações para um novo acordo com a UE e, nas fases seguintes, é provável que o Reino Unido chegue a acordos diferentes com Estados soberanos e outros blocos comerciais. Neste sentido, há a possibilidade de que um futuro acordo Reino Unido - UE e Reino Unido-MERCOSUL precise considerar se o ISDS ou o ICS será adotado. Além disso, o MERCOSUL precisará considerar qual sistema estará disposto a adotar no futuro, caso seja adotado um acordo de disputa entre investidores e Estados, e poderia mesmo explorar um sistema que inclua aspectos tanto do ISDS como do ICS.

Palavras-chave: Sistema de Tribunais de Investimento (ISDS), Lei de Investimentos, Acordo de Livre Comércio, Tribunal Multilateral de Investimentos, MERCOSUL.

RESUMEN BIOGRÁFICO

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