Input of the National Association of Manufacturers (NAM) to the EU Consultation on Investor-State

Question 1: Scope of the substantive investment protection provisions

In an increasingly global and integrated world economy, international investment takes many forms, both in terms of the actual type of assets involved and the ownership structure. Recognizing this fact, both U.S. and EU member state investment instruments have long included broad definitions of investment and we urge the European Commission to adopt a broad definition of investment in its talks with the United States.

A broad definition of foreign investment should include all assets owned or controlled, whether directly or indirectly, that form the basis of an investment, such as the following:

- an enterprise;
- shares, stock, and other forms of equity participation in an enterprise;
- bonds, debentures, other debt instruments, and loans;
- futures, options, and other derivatives;
- turnkey, construction, management, production, concession, revenue-sharing, and other similar contracts or agreements;
- intellectual property rights;
- licenses, authorizations, permits, and similar rights conferred pursuant to domestic
- other tangible or intangible, movable or immovable property, and related property rights, such as leases, mortgages, liens, and pledges.

All of these categories of investment, and others that bear similar characteristics, should be covered by all provisions of the final investment chapter to ensure that investment is appropriately covered. Given the increasing use of technology and advanced manufacturing, as well as complex investment structures, it is critical that intangible forms of investment, such as intellectual property rights, concession or other contracts and agreements, receive the same levels of protection as more tangible forms of property. In the case of investment agreements between a foreign investor and host government (whether those agreements take the form of concession, turnkey, construction or other contracts or agreements), the alleged breach of such an agreement by a host government should also be covered under the ISDS provisions as they are through the umbrella clause of EU member state BITs and through the 2012 U.S. model BIT. The scope of protections should apply to all products and sectors.

Equally important to manufacturers is to ensure that the wide-ranging types of ownership structure in foreign investments be accorded full protection. Investment may be wholly or partially owned or controlled, and that ownership may be direct or indirect. As with EU member state BITs and the 2012 U.S. Model BIT, each of these forms of

ownership structure should qualify an investment or investor to bring an ISDS case. The U.S. model, contains strong provisions preventing misuse or abuse of these rights. In particular, Article 17 of the U.S. instrument authorizes the non-application of the BIT's provisions to an "enterprise that has no substantial business activities in the territory" of the host government and the enterprise is owned by persons of a non-Party. This provision represents an appropriate example of preventing non-investors from taking advantage of the investment provisions provided.

Question 2: Non-discriminatory treatment for investors

Core to investment treaties around the world is the basic requirement that governments not discriminate against foreign investors either compared to domestic investors or investors from third countries. These provisions have been memorialized in U.S. and EU member states BITs through national treatment and most-favored-nation (MFN) provisions. These provisions are critical to include in the investment chapter of the U.S.-EU agreement.

Exemptions from these core non-discrimination provisions should be limited. Furthermore, the EU should also avoid the inclusion of any general exemption or product-or sector-wide exemption to these rules. Those types of exceptions have long been excluded from modern EU member state and U.S. investment instruments given that such exceptions are too easily abused and vitiate the underlying obligation. In regulating in the public interest, there is no justification for discrimination on the basis of the nationality of the investment as such regulation should typically apply equally to domestic as well as foreign investors. Where it may not, the EU can take a tailored non-conforming measure. With regard to EU interest in limiting the application of most-favored nation status through clarification, any such approach is short sighted. As the fundamental purpose of investment negotiations is to liberalize and foster an increasingly open climate that welcomes foreign direct investment, the host country should extend provisions it chooses to grant in future agreements to all foreign investors protected by previous agreements entered into by the same host government.

Question 3: Fair and Equitable Treatment

Fair and equitable treatment (FET) is an essential and indispensable provision in investment instruments worldwide and should be included as a strong feature of the T-TIP investment chapter as well.

Among scholars, the FET standard is regarded as "the most common general absolute standard of treatment in the BITs"[1] and it has long been noted that "[n]early all

[1] Kenneth J. Vandevelde, **Bilateral Investment Treaties: History, Policy, and Interpretation** (2010) at Sec. 5.2.

recent BITs require that investments and investors covered under the treaty receive 'fair and equitable treatment.'"[2] As recognized in the Consultation, the FET standard is contained in nearly all European BITs. It is also included in all modern U.S. BITs[3] and has long been in wide use by multilateral organizations and in other instruments.[4] For businesses in Europe and the United States, this principle is among the most valuable.

The widespread use of the FET standard reflects the fact that it is viewed as a longstanding and basic principle of government behavior towards property and property-owners. This basic principle is widely reflected in the domestic legal regimes of most countries, including the United States, EU and EU member states. Extending the FET in investment instruments extends these domestic guarantee to foreign investors in the same manner as they are provided domestically. In the United States, Constitutional provisions on Due Process, Ex Post Facto laws, Equal Protection, Contracts clause and administrative law provisions, such as the Administrative Procedure Act's limit on "arbitrary and capricious" government action are all reflective of the fundamental nature of the importance of the FET principle. As the Commission itself recognizes, the FET standard is included in most modern investment instruments, including those of the United States and EU member states. It is also a basic principle in international law that has been recognized from the Havana Charter[5] to the current work of the Organization for Cooperation and Development (OECD).[6]

Until the last decade, the typical FET provision in investment instruments was generally very similar, as shown by the examples of the United Kingdom-India:

> "Investments of investors of each Contracting Party shall at all times be accorded fair and equitable treatment and shall enjoy full protection and security in the territory of the other Contracting Party."[7]

and the 1994 U.S. Model BIT:

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[2] Rudolf Dolzer & Margrete Stevens, **Bilateral Investment Treaties** 58 (1995).
[3] *See, e.g.*, id.
[4] Vandevelde, section 5.2.2 (Noting that similar language was used in the Havana Charter and the Organization of American States Charter in 1948, in Friendship, Commerce and Navigation (FCN) Treaties being negotiated by the United States in the 1950s, including the U.S.-German FCN of 1954 which fully incorporated this standard).
[5] The Havana Charter that sought to create the International Trade Organization in 1948, viewed the purpose of the ITO as making recommendations to "to assure just and equitable treatment for the enterprise, skills, capital, arts and technology brought from one Member country to another."
[6] The OECD's Draft Convention on the Protection of Foreign (1967) included as a core protection "just and equitable treatment." As well, 1998 OECD draft multilateral agreement on investment also included language on "fair and equitable treatment."
[7] *See, e.g.*, Agreement Between the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of India for the Promotion and Protection of Investments, March 14, 1994 (entered into force January 6, 1995), Art. 3(2).

> Each Party shall at all times accord to covered investments fair and equitable treatment and full protection and security, and shall in no case accord treatment less favorable than that required by international law."

As originally developed, then, the FET standard sought to protect investors from the full range of unfair and inequitable government behavior, be it bad faith arbitrary or discriminatory action in which any part of a government may engage. This tracks with the description of this standard by the United Nations Conference on Trade and Development (UNCTAD):

> [I]t is possible to identify certain forms of behaviour that appear to be contrary to fairness and equity in most legal systems and to extrapolate from this the type of State action that may be inconsistent with fair and equitable treatment, using the plain meaning approach. Thus, for instance, if a State acts fraudulently or in bad faith, or capriciously and willfully discriminates against a foreign investor, or deprives an investor of acquired rights in a manner that leads to the unjust enrichment of the State, then there is at least a *prima facie* case for arguing that the fair and equitable standard has been violated.[8]

In recent years, however, the United States and a few other countries have moved to restrict the scope of this standard in reaction to concerns that the FET standard was too broad, although in fact there is no evidence that it was applied in an overbroad manner.[9] The U.S. approach adopted in 2004 (and for free trade agreements with Chile and Singapore) defines the FET standards as part of the "customary international law minimum standard of treatment of aliens" and provides further context by stating that:

> "fair and equitable treatment" includes the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world; and

The recent CETA, as presented in the Consultation, defines FET as a measure or series of measures that constitutes:

> a. Denial of justice in criminal, civil or administrative proceedings;
> b. Fundamental breach of due process, including a fundamental breach of transparency, in judicial and administrative proceedings.
> c. Manifest arbitrariness;

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[8] U.N. Conference on Trade and Development, **Fair and Equitable Treatment** 12 (UNCTAD Series on Issues in Int'l Invest. Agrs.) (1999).

[9] Parvan Paravanov & Mark Kantor, "Comparing U.S. Law and Recent U.S. Investment Agreements: Much More Similar than You Might Think," **Yearbook on International Investment Law and Policy** (2010-11) (Includes extensive discussion of fair and equitable treatment cases).

d. Targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief;
e. Abusive treatment of investors, such as coercion, duress and harassment; or
f. A breach of any further elements of the fair and equitable treatment obligation adopted by the Parties in accordance with paragraph 3 of this Article.

The NAM strongly urges that the EU and United States seek the more traditionally broad standard of FET that is consistent with each government's domestic legal principles and one that is not so narrow as to undermine its purpose.

We strongly believe that there are problems with both the U.S. and EU approaches in this regard. The CETA approach limits the FET obligation "only for breaches of a limited set of basic rights" identified above, which would undermine this broad and longstanding core principle. While there is a provision for the parties to identify other actions, that approach is impracticable and fails to take account the evolving nature of state practice. Limiting the FET obligation in the T-TIP would provide U.S. and EU investors with a lower standard than other investors from other countries already enjoy through pre-existing investment agreements. Rather than raising standards, such a result would create a lower standard going forward.

In the case of the U.S. Model BIT, its description of the standard as a non-exhaustive list is much more in line with the longstanding FET principle that was adopted over decades by both the United States and EU member states. However, the U.S. approach limiting the FET standard as a subset of customary international law serves to unnecessarily limit the application of this protection. A far preferable approach would be to provide the FET standard as one in addition to an obligation that the government provide treatment no less favorable than customary international law.

The rationale given for the change in approach was to address critiques that a broad application of the FET standard might somehow undermine a government's right to regulate in the public interest. As discussed more below in response to question 5, neither the FET standard nor other traditional investment treaty standards prohibit the bona fide, nondiscriminatory exercise of traditional government police powers or burden the legitimate exercises of regulatory authority any more than do domestic law standards in Europe and the United States requiring that regulation not be discriminatory, arbitrary, in bad faith, or capricious. As the Commission itself has recognized, government regulatory action cannot be taken in a manner that violates fundamental rights. That too is what the FET standard and other BIT standards require. To the extent that there are legitimate concerns about the use of this or other standards, we strongly believe that they are best addressed through procedural mechanisms, such as provisions to eliminate frivolous claims.

Question 4: Expropriation

Like non-discrimination and FET, compensation for expropriation is a fundamental protection accorded by national governments and long included in international investment instruments. In Europe and the United States, such protections apply to both direct (physical) and indirect (regulatory) expropriations for a public purpose and require prompt, adequate, and effective compensation provided in a non-discriminatory manner and in accordance with due process.

These basic property right provisions have long been included in U.S. and EU member state investment instruments and the investment instruments of most other countries. The NAM urges that similar provisions be included in the T-TIP.

Furthermore, the NAM urges that the proposed EU exclusion of certain measures from the indirect expropriation provision should be rejected. Such an approach is similar to a general exception and would vitiate the purpose of this protection. If more clarification is required, the EU should consider the approach adopted in the 2004 and the 2012 BITs, in which the United States identifies factors that an ISDS panel should consider in making its determination. Such factors include whether the measure is non-discriminatory and whether the measure is manifestly excessive in light of its purpose. The U.S. Expropriation Annex approach provides a useful example of this approach in the context of indirect expropriation, although the provisions in that annex are far less protective of investors in the United States than U.S. Takings jurisprudence, which governs U.S. expropriation issues at the federal level.

Question 5: Ensuring the Right to Regulate and Investment Protection

Investment protections from FET to compensation for expropriation are all longstanding principles of both domestic U.S. and European legal systems and international law. Such standards, like domestic law, provide limited constraints of governments to protect fundamental rights. In negotiating these investment instruments from their earliest days, EU member states and the United States have long ensured their own right as sovereign states to regulate in the public interest. In no way do these investment instruments undermine a government's legitimate right to regulate in the public interest, including to promote health, environmental, safety and public welfare objectives. Further substantive provisions beyond what are included in the U.S. Model BIT 2012 are not needed.

Critiques of investment provisions have become louder through the last two decades, but they are based on false premises and conclusions. Critics of several NAFTA cases, for example, routinely ignore the facts and the outcomes and ignore that

not one single NAFTA case has undermined a government's legitimate right to regulate in the public interest.[10]

Proposals to exempt public welfare measures through a general exception type mechanism or additional language beyond the U.S. 2012 Model BIT would vitiate the purpose and effect of the investment protections. Governments are presumed to be regulating on behalf of the public welfare, but need to follow other basic principles in doing so. The balance required in this area is already well reflected in the standards used in EU member state BITs and in the U.S. model BIT.

Blanket exceptions for environmental, health or other public welfare regulation or any product- or sector-specific exclusions would undermine the very purpose of these instruments. Consider how allowing governments to expropriate, or otherwise treat unfairly green technology in the name of environmental outcomes would affect the industries and jobs that they provide in Europe and America. Given that an expropriation by definition must be for a public purpose, using a general exception in this case would entirely vitiate this provision. Similarly, there is no reason to discriminate against producers by nationality or treat foreign investors unfairly to support public welfare.

In this respect, it is important as well to note that the standard that the United States and EU set in this agreement will be viewed and likely followed by others, including countries with which both the EU and United States are negotiating.

In regards procedural provisions identified by the Commission, we welcome a proper and fair frivolous claims mechanism built in a manner similar to that U.S. Model BIT. On the proposal to develop an appellate mechanism, there has been much discussion of this issue in the United States and globally. Currently, the International Center for the Settlement of Investment Disputes (ICSID) has an annulment mechanism providing appeal on specified grounds.[11] Based on the experience under investor-state cases, there remain questions about the utility of an appellate mechanism. If one is adopted, it is important that any such new proposal not unduly delay the ability of an aggrieved investor to

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[10] See, e.g., Gary Sampliner, "Arbitration of Expropriation Cases under U.S. Investment Treaties – A Threat to Democracy or the Dog that Didn't Bark?" **ICSID Review Foreign Law Journal**

[11] Article 52(1) of the ICSID Convention provides:

> Either party may request annulment of the award by an application in writing addressed to the Secretary-General on one or more of the following grounds:
> (a) that the Tribunal was not properly constituted;
> (b) that the Tribunal has manifestly exceeded its powers;
> (c) that there was corruption on the part of a member of the Tribunal;
> (d) that there has been a serious departure from a fundamental rule of procedure; or
> (e) that the award has failed to state the reasons on which it is based.

achieve a conclusion in the case, which are already highly time-consuming and expensive, lasting oftentimes several years.

Question 6: Transparency in ISDS

The NAM generally welcomes increased transparency in the ISDS process, as we support transparency more generally with respect to government action. The EU's proposal to require transparency in consultations, pleading and hearings is generally consistent with the approach adopted by the United States in a clarification to NAFTA and then in the 2004 and 2012 Model BITs, which the NAM supports.

The NAM does want to emphasize that transparency provisions should not put at risk the release of business confidential information and welcome the EU's recognition of this important principle. The NAM also believes it is critical that the transparency provisions be applied in a manner that does not result in undue burdens or abuse the process.

Question 7: Multiple Claims and Relationship to Domestic Courts

The NAM believes it is critical that an investor or investment have the choice of a domestic court or ISDS tribunal, and welcomes the EU approach in offering incentives to promote the use of domestic courts, such as increased time to file an ISDS case. At the same time, it is important to note that such provisions should not lock an investor into a domestic court proceeding, including through proposals that investors exhaust local remedies before proceeding to an ISDS panel. Such a result is contrary to the purpose of the ISDS process to allow an investor to leave a local tribunal where it does not believe it can get a fair hearing. Such exhaustion proposals would also add substantial time and cost to the consideration of claims for both the investor and the host government.

The NAM also supports the EU proposal, which is reflected in the U.S. approach as well, that a claimant should not receive duplicate awards for the same harm or prosecute the same claim at the same time in both domestic courts and ISDS panels.

Question 8: Arbitrator Ethics, Conduct and Qualifications

The NAM agrees that ISDS panels should include independent arbitrators that have expertise in international arbitration law and adhere to high ethical standards. While the current system has largely operated according to such standards, more detailed processes to promote the use well qualified, unbiased and ethical arbitrators may help instill stronger support for this longstanding

arbitration process. Providing more systemic procedures to prevent conflict of interests similarly may help promote stronger confidence.

It is important that the standard process for choosing arbitrators – in which each of the two parties designates an arbitrator and then those two arbitrators choose the third arbitrator – remain the same as it has generally worked well. Efforts to unduly restrict the choice of arbitrators that meet the core independence, qualification and ethical standards should be rejected.

Question 9: Reducing the Risk of Frivolous and Unfounded Claims

The NAM generally supports procedures, as reflected in the U.S. Model BIT, that permit ISDS panel to reject claims that do not state a valid claim or lack a jurisdictional basis based on appropriate criteria. Although this has not appeared to be a significant problem in investor-state cases, it does reflect an appropriate exercise of arbitral authority.

The EU proposal to award attorney fees automatically to an investor whose claim has been rejected under that standard is, however, overly far reaching. While an ISDS panels appropriate retains that authority, it should not be automatically applied in any case.

Question 10: Allowing Claims to Proceed (Filter)

In general, the NAM opposes any filtering mechanism that denies investors access to neutral dispute settlement for valid claims under the terms of an investment instrument. As explained above (in response to question 5 and the right to regulate), the basic protections accorded investors and investment in the typical text do not undermine a government's right to regulate appropriately in the public interest

The U.S. Model BIT has a prudential carve out with respect to financial services, which the EU appears to be interested in adopting. This provision, while relatively well-crafted, still puts at risk industries that may have valid claims that the home and host governments seek to prevent from being considered. The NAM would urge the EU to reject consideration of a prudential or any other type of filter mechanism in the T-TIP.

Question 11: Guidance by the Parties (the EU and the US) on the interpretation of the agreement

While the NAM recognizes the interest of the home and host government to help provide guidance with respect to the interpretation of investment provision,

proposals to provide for binding government interpretations during the conduct of individual ISDS cases or more broadly is concerning. Such proposals suggest that the governments could change the terms of previously approved agreements, contrary to the fact that such agreements were fully implemented (oftentimes by different branches of government).

Question 12: Appellate Mechanism and Consistency of Rulings

Over the past decades, there has been increasing discussion of the potential development of an appellate mechanism for ISDS cases. Given the over 3,000 treaties, with differing terms, there is less than a clear consensus on whether such an approach would in fact create greater consistency in rulings by ISDS panels. From a business perspective, there is no strong reason to adopt an appellate mechanism. To the contrary, such a mechanism is widely viewed as unnecessary and likely to increase substantially the time and cost of arbitration procedures.

Question 13: General Assessment

Investment is a critical driver of economic growth and jobs in both the United States and EU, and in third countries around the world. The United States and EU have an important opportunity to set high standards for the protection of property and investment through the T-TIP that reflect our own core principles and help influence investment instruments being negotiated around the world.

The investment treaties and experience of EU member states and the United States has been highly positive, reinforcing basic rule of law standards with our international partners. The overall strength of these investment instruments are important markers of the United States' and EU's embrace of the rule of law and strong enforcement. While a lot of critiques have been made, the facts are very clear. U.S. and EU investment instruments are not a threat to good government; in fact, they promote it and promote growth and jobs as well.

The EU should consider not only the strongly positive experience of its member states with investment instruments, but also look forward to the type of standards that the EU and its stakeholders hope to achieve with major economies around the world, from India to China. In considering the past, the present and the future, we believe that the adoption of the strongest possible provisions to protect and promote investment, subject to strong enforcement mechanisms, is the best outcome for the EU and the United States.