



Trade deals: Toxic talks

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Critics claim that international arbitration has morphed into a weapon that multinationals wield to threaten and influence

Australia's insistence that cigarettes be sold in drab olive packaging with warning labels featuring tar-stained lungs and malignant tumours set a precedent for public health officials around the world. With a substantial decrease in the number of Australians lighting up and other countries such as France, Ireland and the UK poised to follow suit, the health policy battle seems largely won.

But the impact of Australia's 2011 plain packaging law is reverberating far beyond the world of public health. The battle provoked by the law change has strayed in to global trade and investment policy.

Shortly after the measure passed parliament, the tobacco industry began a legal assault that continues to this day. Cigarette makers filed a suit in Australia calling the new law unconstitutional. Countries such as Indonesia and Ukraine – siding with the tobacco industry – brought cases against Australia in the World Trade Organisation, arguing that it violated global trade rules.

But the industry also took a second, more unconventional legal avenue. In June 2011, shortly after the law was agreed, tobacco group [Philip Morris International](#) invoked the dispute clause in a 1993 investment treaty between Australia and Hong Kong. Unless an “amicable settlement” could be found, it said, it would circumvent the Australian legal system and seek compensation before an international arbitration panel for what it called the government's “expropriation” of its intellectual property.

By neutering its brands, Australia had destroyed the value of its investments in the country, the tobacco company claimed, adding: “Legal action is not a course we take lightly, but the government has unfortunately left us with no other option.”

The case remains unresolved. But its importance has grown in the past three years amid an escalating global debate over the role international arbitrators should play in deciding, or resolving, investment disputes between countries and multinational companies.

Business groups insist the global arbitration system, in place for more than 50 years and shaped, by some 4,000 bilateral investment treaties, offers legal protections to foreign investors. Without it, they say, investors are vulnerable to local court systems and the whim of governments.

However, a growing number of critics point to a surge in cases over the past decade arguing the system has morphed from a legitimate way for foreign investors to challenge extreme injustices such as expropriations, into a way for them to threaten, or influence, government regulations and even policy.

In the past year Indonesia and South Africa – both of which have been on the receiving end of punitive judgments in investor arbitration cases – have said they would either end, or allow to expire, all their [bilateral investment treaties](#) containing such dispute clauses.

The threat comes as the US, EU, Japan and other big economies seek to complete trade agreements that include protections for investors. The debate looms large over the [EU-US trade talks](#). It casts an even longer shadow over investment negotiations with China, where foreign companies are coming under increasing – and some argue unfair – regulatory scrutiny even as Beijing complains about the treatment its own companies receive overseas.

The debate is at its [most lively in Europe, where](#) the European Commission is wading through more than 150,000 submissions after a public consultation on its plans to include what is technically known as an “investor-state dispute settlement” or ISDS, in the US agreement. Germany has already said it will seek to strip out the right of foreign investors to seek international arbitration from an EU trade deal nearing conclusion with Canada and the far-bigger one being negotiated with the US.

How in the world can the US and Europe expect the rest of the world to be bound by investment rules if they are not?

When Cecilia Malmström, the Swede set to become the EU’s next trade commissioner, appeared before the European Parliament for her confirmation hearing last week she spent most of it fending off questions on ISDS.

“It is indeed a very toxic issue in this parliament and elsewhere,” Ms Malmström told the international trade committee.

In the hearing she suggested the ISDS mechanism could be left out of the [pact with the US, but made clear](#) that she believed they were a legitimate means of settling commercial disputes.

“I agree that there are problems with ISDS because there have been abuses,” she told the trade committee. “But [investment treaties] exist. We can’t just think them away globally.”

American officials remain convinced of the need to include investment protections in any transatlantic pact. They also insist – as does Ms Malmström – that the goal is to close loopholes in existing bilateral deals and set a high standard for future trade agreements.

James Bacchus, a former Florida congressman who heads the International Chamber of Commerce’s committee on investment policy, says the system works better than its critics allow. While opponents have latched on to cases such as Philip Morris’ against Australia the fact is, Mr Bacchus says, that most rogue cases do not succeed.

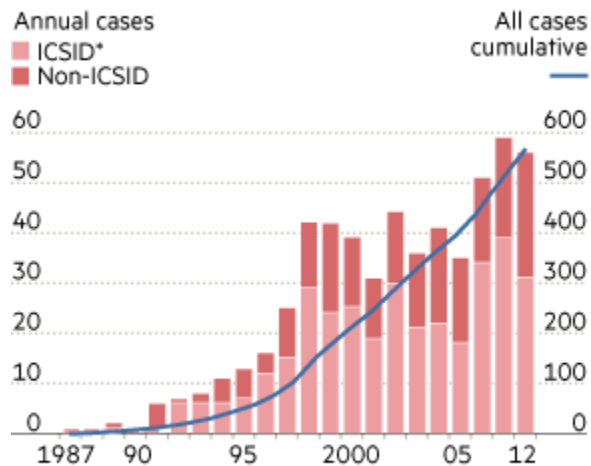
“It is very easy for lawyers to invent reasons to bring a lawsuit. It is much harder for them to win one,” he says.

More importantly, he argues, that, with investment negotiations looming with China, both the EU and the US need to stay their course.

“How in the world can the US and Europe expect the rest of the world to be bound by investment rules if they are unwilling to be bound by investment rules themselves?” he says.

Over the past six decades EU member countries have signed more than 1,400 bilateral investment treaties, the vast majority of which allow for investors to seek international arbitration in the case of disputes. And EU companies account for most of the cases filed using ISDS mechanisms. According to the UN Conference on Trade and Development, by the end of 2013, 568 ISDS cases involving 98 countries had been filed. EU companies were responsible for more than half of those cases.

In court: ISDS cases



* The International Centre for Settlement of Investment Disputes

Source: UNCTAD

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But the system remains opaque, masking its success or failure rate. That murkiness is part of a bigger problem. Owing to the vague nature of the dispute clauses in many existing treaties, they have often been open to abuse. Hearings, documents and judgments often remain private. They also contain loose definitions of grounds under which foreign investors may seek compensation.

Taken together, those loopholes have allowed lawyers to exploit the system and led to a surge in cases, critics argue.

The European Commission, which gained responsibility for EU investment policy in 2009, argues it is trying to clean up the mess with new agreements.

The first dispute resolution mechanism negotiated by the EU – in the deal with Canada – runs to 22 pages and includes requirements for all hearings and documents to be public. But critics argue it still allows multinationals to circumvent local courts and raises the possibility of many more cases.

The problem, says Matthew Rimmer, a law professor at Australian National University, a leading critic of investor protection clauses, is that too many areas of government remain open to challenges. “The troubling thing with all those agreements is they still have an expansive view of what an investment is,” he says.

Critics argue this can lead to “regulatory chill” where governments, afraid of having to fight such cases, stop themselves from introducing regulations or passing laws.

That fear is fuelling European criticism. In Germany much of the opposition to the clauses has sprung from a case brought by Vattenfall, the Swedish energy group, over the abrupt changes in policy that [Berlin pushed through](#) after the 2011 Fukushima nuclear disaster in Japan.

In France environmentalists have raised the prospect of US oil companies suing under a transatlantic trade pact’s ISDS clause to overturn future bans on “fracking” for shale gas or oil. British trade unions say they fear the potential impact on the National Health Service. The simple threat of multi-million-dollar lawsuits brought before international arbitration panels, they argue, might pre-empt any efforts by future governments to keep drug prices low, for instance.

The problem business groups and other advocates face is that the opposition is increasingly organised and drawing together sometimes unexpected ideological bedfellows.

Liberal economists such as Nobel laureates Joseph Stiglitz and Paul Krugman argue that ISDS mechanisms undermine the sovereignty of nations. The libertarian Cato Institute has also weighed in to demand that investor protections be stripped out of a proposed EU-US pact.

Daniel Ikenson, who heads the Washington-based think-tank’s trade division, argues that investor protections in bilateral treaties and trade agreements amount to a corporate subsidy that has encouraged the “discretionary offshoring” of American jobs. He also argues that they ought to be ditched from trade talks because they have become such an obsession of anti-globalisation activists that they are now “toxic”.

Critics such as Mr Stiglitz point out there are plenty of other options for businesses to insure against political risk when they make foreign investments. The World Bank houses the International Centre for Settlement of Investment Disputes, where many of the ISDS cases in the world are heard.

There is also a legitimate question over just how much investment treaties – and investor protection clauses – do to lure foreign investors. Neither Brazil nor China have many treaties in place, yet both have attracted enormous amounts of foreign direct investment.

UN economists studying whether investment treaties promote FDI found that other factors were often more important. Investment agreements “cannot substitute for sound domestic policies,” the UN Conference on Trade and Development found.

Six years after the global financial crisis it is hard to find a government that is not going out of its way to lure foreign investment. Even as the debate on just what they have to do to attract investors, and what protection they need to offer them, is only really getting started.

Germany: The chicken that sparked a trading spat

Nowhere is the debate over the EU’s planned trade pact with the US more passionate than in [Germany](#). And nothing has stimulated more passion than the humble chicken, *writes Stefan Wagstyl*. Transatlantic Trade and Investment Partnership critics claimed that the proposed deal would open EU supermarkets to chlorine-washed US chickens. They insisted such birds were a consumer health risk.

It took chancellor Angela Merkel’s personal intervention to lick the chicken campaign: she promised that the pact would not affect the EU’s chlorine-washing ban.

But her pledge has done little to slow the anti-TTIP campaign. The critics are now focusing their attacks on investor protection rules, which would allow companies to appeal to international tribunals. The campaign’s energy has created the impression that Germans are against TTIP. They are not. A Pew Research poll this year showed 55 per cent backed the pact, with 25 per cent against. But with a further 20 per cent uncertain, TTIP’s opponents sense there is plenty to fight for.

Ms Merkel’s government is committed to TTIP and to the Comprehensive Economic and Trade Agreement, the planned trade pact with Canada. But the agreements require parliamentary approval, so creating hope for critics.

The parliamentary assaults are spearheaded by the opposition Linke, the far-left party, with some support from the Green party, which wants a rethink of both deals to give more weight to consumers’ rights.

The campaigners appeal to popular concerns about globalisation, the infringement of sovereignty, and the protection of consumers, workers and the environment. Sahra Wagenknecht, Linke’s deputy parliamentary chief, said: “Fundamentally, these undemocratic free trade agreements which threaten the general good must be stopped.”

The anti-TTIP lobby has also capitalised on a resurgence of anti-Americanism driven by whistleblower Edward Snowden’s revelations of widespread US secret surveillance.

TTIP's backers are led by Ms Merkel's CDU/CSU conservatives, who argue that Germans will benefit hugely from the increased trade the pact would bring and the opportunity to develop global commercial standards, including for investor protection. Michael Grosse-Brömer, the CDU chief whip, told the Financial Times: "The biggest advantage is that when the EU and the US make this deal, it will include standards which can be applied worldwide." The BDI, the German business association, says that investor protection is "essential" for export-oriented German companies.

However, Ms Merkel's social democrat coalition partners are divided. Sigmar Gabriel, vice-chancellor, told parliament last month that while free trade was good, investor protection rules would give "unnecessary" and "unfair" extra help to multinationals.

The SPD is split between globalisation-wary leftwingers and rightwingers worried that a failed TTIP could hurt the EU's economic clout and damage transatlantic ties. As a former SPD minister says: "If TTIP collapses, the political backlash could last 10 years."