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Article

## Courting balance between investor and host state in ISDS

By **R Subhashree**

The India's model BIT (Bilateral Investment Treaty) was criticised as moving away from investor protection and being unreal. Foreign investor protection and the Investor State Dispute Settlement (ISDS) mechanism have received lot of attention, of late and has triggered law suits in the national courts [*Hupacasath First Nation* v. *Canada*], public consultation by European Commission besides host of representations and campaigns cautioning against compromising the right of sovereign governments to legislate/ regulate and making the foreign investor more than equal as compared to a domestic investor though the treaty language calls for 'National Treatment'.

### *Showing the way (EU) or doing away with 'foreign' investor claims(South Africa)*

Two solutions are being debated currently and are interesting for the difference in approach. The European Commission (EC) has proposed an international investment court modelled on the WTO dispute settlement mechanism while South Africa seeks to revoke all its existing BITs and adopt national legislation as a means to assure protection for investments. While South Africa seeks to bring the entire issue within the folds of domestic law guaranteeing equality as per its constitution, the EC seeks to remedy the issue by improving the procedure of how an investor is compensated. It is interesting that the arbitration model which was advanced as an effective and quick remedy for expropriation is being brought within the more traditional judicial process to improve its efficacy and acceptance.

The EC identified four areas for improvement based on its consultations - protection of the right to regulate; establishment and functioning of arbitral tribunals; review of ISDS decisions through an appellate mechanism and the relationship between domestic judicial systems and ISDS.

### *Drafting and appeal*

The EC envisages an operational provision in the treaty specifically worded to protect right to regulate in public interest, establishing a roster list of arbitrators which are agreed to by the parties (States) in advance, conferring right to third parties with direct interest in the dispute, to intervene and an appeal mechanism. It calls for setting up an appellate body with 7 permanent members whose qualifications could be broadly similar to those of the WTO Appellate Body and/or the International Court of Justice. The EC proposal seeks to avoid multiplicity of proceedings by asking parties to choose between national law and arbitration and barring arbitral tribunals from reviewing decisions of national courts. The EC proposes that EU should pursue the creation of one permanent court which would later become multilateralised as a self standing international body or by embedding it into an existing multilateral organization. The EC

proposal also seeks to improve the drafting of the treaty so that wide interpretation is rendered impossible. It seeks to address the problems of bias of arbitrators, restricting frivolous claims by arguing against 'loser pays' principle. The first response from the US, with whom EC is negotiating the Transatlantic Trade and Investment Partnership (TTIP), has been negative.

### *Making the foreign investor 'Equal'*

South Africa's 'Promotion And Protection of Investment Bill 2013' (PPIB) and the 'Expropriation Bill' clarifies its stand on the issue of investor protection against expropriation. For the first time, the domestic investor will have a right / be eligible to be compensated and rather than resorting to a treaty obligation which means that (foreign) investor protection will have the backing of domestic laws. The Expropriation Bill sets out a procedure for appropriation with due notice etc, calculation compensation due and determination of the by the court in certain cases. Expropriation may be for public purpose or in public interest. The PPIB provides for national treatment, reiterates sovereign right to regulate in public interest to correct historical inequalities and provides for dispute resolution by arbitration or mediation without specifically mentioning international arbitration or bodies like ICSID or UNCITRAL. The Bill also states that compulsory licensing, measures having adverse effect without permanent ownership being transferred to the State shall not be expropriation and compensation need not be provided to the investor.

### *Weighing the approaches*

As can be expected, each country's proposal is a response to the issues faced by it. For instance, wording pertaining to addressing historic inequalities is a fallout of the challenge to grant of mining rights which were held by a foreign investor, to historically disadvantaged South Africans to promote better sharing and access to South Africa's resources. [*Piero Foresti, Laura de Carli and others* v *The Republic of South Africa*, ICSID Case no ARB(AF)/07/01]. Among the member countries of EU, almost 1400 BITs are in existence and seen as encouraging bilateral investment and hence it does not want to and may find it impossible to scrap them altogether.

The EC proposal is appealing since it envisages a WTO like body which can be successful but if there is to be an appeal mechanism, funding of a permanent court etc, time and cost involved will still make it unattractive to the investor and host state respectively. Some critics of the EC proposal also argue that without a well-drafted treaty, no amount of fair interpretation will come to the aid of the host state. Without a treaty obligation as per the South African model, investors will be hesitant since there is little guarantee that the State will not change its laws at a later date.

Earlier this year UNCTAD organised a meeting to discuss how the investment dispute settlement process can be reformed. The differing views which emerged essentially question the balance between efficacious

remedy for a foreign investor who can have a say in the arbitration process and the remedy through an investment court which raises question of who will fund the same, whether it will have jurisdiction over investment contracts, etc. The public discussion draft released by OECD on BEPS suggests mandatory arbitration as a means to effective dispute resolution so that Mutual Agreement Procedure (MAP) for cooperation between the tax authorities of different countries can provide quick remedy. However, not many member countries are in favour of the same.

### *Refining the treaty text*

We still do not have an answer on the best method to ensure investor protection without compromising on certain sovereign rights of a state. The questions still remain – how much protection should a foreign investor get, what would amount to expropriation, how much compensation should be paid to an investor and who should decide? May be the answer lies in drafting the treaty without vague terms and clauses like the MFN which is used to import more favourable terms from other treaties. After all, the basis for claims and the framework for dispute settlement arise from treaties. For instance, though it is not used often, the non-violate clause in WTO agreements seeks to protect impairment of benefits caused by '*existence of any other situation*' - even when the action does not conflict with any provisions of the agreement. The use of such terms is open to broad interpretations. Any dispute settlement forum will look to the treaty for interpretation and hence the better option is to concentrate on the drafting of the terms.

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## Trade Remedy News

### *Trade remedy measures by India*

| Product | Country | Notification No. | Date of Notification | Remarks |
|---|---|---|---|---|
| Caustic Soda | China and Korea RP | 15/23/2013-DGAD | 18-6-2015 | ADD sunset review recommends continuation of duty |
| Digital Offset Printing Plates | China | 15/27/2013-DGAD | 3-7-2015 | ADD mid-term review terminated |
| Flax Fabric | China and Hong Kong | 15/30/2013-DGAD | 9-6-2015 | ADD sunset review recommends continuation of duty |
| Float Glass | China PR and Indonesia | 15/24/2013-DGAD | 2-7-2015 | ADD continuation recommended on imports from China. Final finding notes insignificant imports from Indonesia. |

| Product | Country | Notification No. | Date of Notification | Remarks |
|---|---|---|---|---|
| Front axle beam and Steering knuckles meant for heavy and medium commercial vehicles | China | 354/118/2009-TRU (Pt-I) | 8-6-2015 | Time for completion of Sunset Review investigation extended till 12-9-2015 |
| Hot Rolled Flat Products of Stainless Steel of ASTM Grade 304 | China , Korea and Malaysia | 28/2015-Cus. (ADD) | 5-6-2015 | Definitive anti-dumping duty imposed |
| Nylon Tyre Cord Fabric (NTCF) | China | 30/2015-Cus. (ADD) | 12-6-2015 | Definitive anti-dumping duty continued for 5 years |
| Phosphoric Acid | Korea RP | 15/7/2014-DGAD | 19-6-2015 | ADD sunset review recommends continuation of duty |
| Plain Medium Density Fibre Board having thickness of 6mm and above | Indonesia and Vietnam | 14/23/2014-DGAD | 22-6-2015 | Time for submission of questionnaire responses extended till 12-7-2015 |
| Plastic Processing Machines | China | 354/53/2009-TRU (Pt-I) | 2-6-2015 | Time for completion of Sunset Review investigation extended till 8-8-2015 |
| Potassium Carbonate | Korea RP, and Taiwan | 15/12/2014-DGAD | 8-6-2015 | ADD sunset review recommends continuation of duty |
| Purified Terephthalic Acid (PTA) | China Iran, Indonesia, Malaysia & Taiwan | 14/8/2015-DGAD | 18-6-2015 | Anti-dumping duty investigation initiated |
| Vitamin-E | China | 29/2015-Cus. (ADD) | 10-06-2015 | Definitive anti-dumping duty re-imposed |

## *Trade remedy actions against India*

| Product | Country | Notification No. | Date of Notification | Remarks |
|---|---|---|---|---|
| Corrosion-Resistant Steel Products | USA | 80 FR 37223 [C-533-864] | 30-6-2015 | CVD investigation initiated |
| Corrosion-Resistant Steel Products | USA | 80 FR 37223 [A-533-863] | 30-6-2015 | ADD - Initiation of Less than fair value investigation |

| Product | Country | Notification No. | Date of Notification | Remarks |
|---|---|---|---|---|
| Hot-rolled carbon steel plate and high-strength low-alloy steel plate | Canada | Canadian International Trade Tribunal Press Release | 10-6-2015 | ADD and CVD investigation initiated |
| Silicomanganese | USA | 80 FR 31891 [A-533-823] | 4-6-2015 | Preliminary Results ADD Administrative review – Absence of sales by specified entity at prices below normal value |

## WTO News

### Ukraine's Safeguard measures on cars found to violate WTO provisions

On 26 June 2015, the WTO issued the panel report in the case brought by Japan regarding *"Ukraine — Definitive safeguard measures on certain passenger cars"* (DS468). Panel here was of the view that Ukraine failed to make a proper determination regarding existence of unforeseen developments and the effect of GATT 1994; did not make a proper determination regarding increased imports, threat of serious injury to the domestic industry and regarding causal link; failed to publish promptly analysis of the case; failed to notify to the WTO Committee on Safeguards; and failed to provide all pertinent information in the notification. Japan's contention that Ukraine failed to provide reasonable public notice and public hearings to interested parties to present evidence, was however rejected by the panel. Ukraine was found to violate Articles 2.1, 4.2, 8.1, 12.1, 12.2 and 12.3 of the Agreement on Safeguards and Article XIX:1(a) of the GATT 1994. The Panel has suggested Ukraine to revoke its Safeguard measures on passenger cars.

### Vietnam disputes Indonesian Safeguard measures on steel

Safeguard measures were also at the centre of dispute between Vietnam and Indonesia. Vietnam has on 1-6-2015 initiated new dispute (DS496) proceeding against Indonesia regarding Indonesia's imposition of a Safeguard measure on imports of flat-rolled products of iron or non-alloy steel. According to Vietnam, measure appears not to be based on proper determination or a reasoned and adequate explanation of any unforeseen developments that led to the increased imports that caused or threatened to cause serious injury to the domestic industry. Violation of Articles 2.1, 3.1, 4.1(a), (b) & (c) and Article 4.2(a), (b) & (c) of the Agreement on Safeguards is alleged by Vietnam in this dispute while also invoking some Articles of GATT.

### Canada's request to suspend concessions in "US - COOL" dispute

Canada has requested Dispute Settlement Body to authorise them to suspend concessions in the amount of about US$ 2.5 billion. The compliance panel of the Appellate Body of the DSB had earlier concluded that the amended US COOL measures continued to be inconsistent with the US obligations under the Technical Barriers to Trade (TBT) Agreement and the General Agreement on Tariffs and Trade (GATT) 1994 (Refer, DS384). The DSB now at its meeting on 17 June considered Canada's request for authorisation to suspend concessions against the United States, and in light of the US objection to Canada's "excessive" request, the matter has been referred to arbitration.

### USA appeals compliance panel report on tuna dispute

In another TBT dispute, the United States has filed Appeal against the compliance panel report in the dispute *"United States – Measures concerning the importation, marketing and sale of tuna and tuna products from Mexico"* (DS381). USA disputes Panel's findings and conclusion that the amended U.S. dolphin safe labelling measure is inconsistent with Article 2.1 of the Agreement on Technical Barriers to Trade because it accords less favourable treatment to Mexico's tuna and tuna product exports.

### Slight deceleration in G20 trade restrictions: WTO report

WTO's Report on G20 Trade Measures shows a slight deceleration in the application of new trade-restrictive measures by the G-20 economies. According to the report dated 12-6-2015 (released on 15-6-2015), average number of such measures applied per month was found lower than at any time since 2013. The Report notes that trade liberalizing measures remained stable with G-20 economies introducing some 112 new measures during the period under review (Mid-October 2014 to Mid-May 2015). Further, of the 1,360 restrictions recorded since 2008, only less than a quarter have been eliminated, despite the G-20 pledge to roll back any new protectionist measures. On the positive side, report notes that growth in the volume of world merchandise trade should increase from 2.8% in 2014 to 3.3% in 2015 and further to 4.0% in 2016.

## Ratio Decidendi

### ADD investigation – Adjustment of commissions paid by manufacturer to related exporter, in export price

European Union's General Court has upheld the downward adjustment to the export price in respect of commissions paid by the manufacturer to its exporter. The applicant-manufacturer here was of the view that they and the exporter (Singaporean entity) formed a single economic entity and that, consequently, there was no need to carry out any downward adjustments in export price to the EU. The council here though did not dispute existence of common control but had

denied presence of single economic entity. The dispute involved imports of certain fatty alcohols and their blends originating in India, Indonesia and Malaysia.

Noting that such an entity can be found to exist only if the functions carried out by the related trader are similar to those of an internal sales department, the court also rejected the plea of presence of single economic entity. Observing that overall functions carried out by the related trader in the marketing and export of not only the concerned product but other products as well, both within the group and in its relations with independent third party producers, have to be examined, the court rejected the plea of single entity noting that overall activities of the related exporter were based to a significant extent on supplies from unrelated undertakings and hence same cannot be considered as internal sales department. The court for this purpose also held that existence of such written contract between the manufacturer and the exporter also demonstrates that the relationship between them is organised on the basis of normal commercial conditions as distinguished from other related companies between which any payment of commissions is based only on a series of verbal agreements.

Relevant clauses of the agreement between the two were also considered by the court in this regard to deny existence of single entity and while rejecting the plea that written agreement is necessary for the purposes of governing transfer pricing between related parties and complying with the recommendations of the Organisation for Economic Co-operation and Development (OECD) on transfer pricing. Further, functions carried out by the exporter were found to be similar to those of an agent working on a commission basis and hence applicability of provisions of Article 2(10)(i) of the EU's Basic Regulation were found to be correct. The court also rejected the plea that similar adjustment to the normal value was also required. [*PT Perindustrian dan Perdagangan Musim Semi Mas (PT Musim Mas)* v. *Council of the European Union* – Judgement dated 25-6-2015 in Case T-26/12, EU's General Court (Seventh Chamber)]

## News Nuggets

### Australia and China affirm free trade

The text of the China -Australia FTA was signed on June 17, 2015. The FTA is expected to bring gains for Australia in terms of better access for dairy sector, horticulture and energy products like coking coal by way of reduced tariff. Australian insurance providers, banks and financial service providers will also benefit from greater access to Chinese markets. Australia will reduce tariffs on Chinese manufacturing exports, electronics and white goods, and will raise the screening threshold for Chinese investments into Australia in non-sensitive sectors though it will continue to monitor investments in agricultural land and agribusiness, and sensitive sectors, including media, telecommunications and

defence-related industries at the current screening levels.

The text incorporates the ISDS provisions with certain variations from standard clauses like the 'Future Work Program' which envisages review and negotiations between the two countries to include articles on minimum standard of treatment, expropriation, etc, within a period of 3 years from the date of the current agreement. Some of the interesting aspects of the FTA is the side letter which confirms Australia's willingness to encourage and support the development of Traditional Chinese Medicine and the MOU whereby Australia will allow overseas workers to be employed in certain infrastructure projects.

## From bounded public interest test to time bound AD

New Zealand continues to seek ways to reform its anti-dumping and countervailing duties regime. Last year it had sought views on introduction of a bounded public interest test (*refer International Trade Amicus, July 2014 issue*) and now proposes to lay down the broad parameters and procedure to take into account the effect of AD, on public - parties other than domestic producers. A supplementary discussion paper issued last month talks about introduction of an automatic termination period (ATP) such that duties are terminated after a set time period and it will not be possible for domestic industry to apply for re-imposition of duties, at least not until a minimum 'stand down' period has elapsed. In its assessment of the pros and cons of an ATP, the discussion paper records that a set period will encourage industries to act within such time to adjust their prices instead extending AD's for longer periods / abusing the instrument of AD. It is proposed that while seeking re-imposition of duties the industry should provide fresh evidence of injury. The paper also records that the proposal for ATP was part of the Doha round though it could not be finalised.

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