To CETA or not to CETA: Reflections on ISDS and the special responsibility of national parliaments

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In a reaction to an EJIL: Talk! post by Baetens et al., Arcuri et al. claim that the Dutch parliament has the right to reject CETA and also argue in favour of it doing so. The post by Arcuri et al. raises important points that merit further discussion, among legal academics and practitioners, politicians, and citizens. We would like to broaden the discussion on three points in particular. First, without questioning the right of the Dutch parliament to reject or endorse CETA, it merits pointing out that the scope of this right is not all encompassing. Second, on the issue of the ISDS regime that is included in CETA we argue that the decision to accept or reject it should be informed by a thorough knowledge of both the law and practice of ISDS. Third and finally, we argue that it is useful to take a step back and ask the question whether comprehensive trade agreements, such as CETA, need to be concluded as mixed agreements to begin with.

1. **The limited scope for national parliaments to reject or approve CETA**

As two of us have argued elsewhere, discussions on the legitimacy of national parliamentary involvement in the ratification of trade and investment agreements negotiated by the EU should start from a sound analysis of the division of competences between the EU and the Member States. Per the principle of conferral, the EU holds only those powers conferred upon it; powers not conferred upon the EU remain with the Member States. As a consequence, issues that fall within the scope of the competences exercised by the EU should be debated at EU level; and issues coming within the scope of competences exercised by the Member States should be debated at the national level.

For CETA, this means that during the national ratification procedures, national parliaments should only debate the agreement's provisions on non-direct foreign investment and the ISDS regime. Conversely, discussions on the protection of halloumi or other regional food specialties—issues which unambiguously fall within the scope of the EU's exclusive competences—should be held within the Council and the European Parliament only. Any national parliamentary debate, in the national ratification procedure, on these issues undermines the prerogatives of those EU institutions, and in particular of the directly elected European Parliament.

2. **The (non-)sense of including ISDS in comprehensive trade agreements**

As a second argument, Arcuri et al. mention that it is legitimate not to ratify CETA because ISDS is "one of the most controversial institutions in the contemporary legal order". The authors then proceed to raise multiple concerns and arguments against having ISDS in CETA, amongst which 'regulatory chill', the system's asymmetric nature, and possible detrimental effects on environmental protection. Whilst it is without doubt that ISDS has gone through a 'legitimacy crisis' over the last decade, the situation is not static. When looking at ISDS, academics should strive to present a more balanced picture, encompassing the 'good, the bad' and possibly the 'ugly.'

Firstly, several empirical projects and the UNCTAD's annual Investment Reports show a more balanced picture in which investors and States win and lose cases in roughly equal proportions (host States winning slightly more cases), an improvement from the situation 2-3 decades ago when investors won most of the cases. There is also no study that we know of which discusses how much of the sums awarded to investors by arbitral tribunals is actually recovered. In this regard one just needs to look at the *Yukos* or *Micula* sagas to appreciate the difficulties of recovering the sums awarded to investors.

Secondly, when it comes to ISDS's alleged negative impact on environmental protection, the picture is once again more nuanced than suggested by Arcuri et al. Behn's and Langford's empirical study on the impact of ISDS on environmental protection concluded that "in a number of important areas, the critiques do have purchase but in the aggregate, the most problematic cases are often successfully defended by respondent states".

Thirdly, whilst it is debatable whether the Investment Court System (the ICS) under CETA is the "gold standard", the ICS encompasses significant improvements compared to the succinctly worded ISDS provisions under traditional, Member State BITs. Just to mention a few of the improvements; the substantive standards, such as Fair and Equitable Treatment, are more carefully defined. Instead of *ad hoc*, party-appointed tribunals, a standing Tribunal and Appeals Body is envisaged. Furthermore, unlike traditional ISDS, there is also the chance of appealing the decision. Whilst it is true that the system is asymmetric in nature, as it only allows foreign investors to use it, EU investors abroad will be able to use it, just as foreign investors investing in the EU. According to the Court of Justice of the EU (CJEU) in Opinion 1/17, this asymmetry should not be confused with (prohibited) discrimination.

Fourthly, it is not readily apparent whether Member States' interests align or are static. Capital exporting Member States have benefited from concluding BITs as their companies have used ISDS against host States (even against other EU members) whilst other EU members have often been on the receiving end of ISDS. This split in Member State interests was made evident by AG Wathelet in his Opinion in the *Achmea* case. However, after having handed over their exclusive competences over foreign direct investment (FDI) to the EU (art. 207(1) TFEU), at least capital exporting Member States will expect the EU to include ISDS in its new agreements. Therefore, investors from a capital exporting country like the Netherlands will continue benefiting from the ICS,

with the possibility that the Netherlands might also face future cases against it, as pointed out by Arcuri et al. Furthermore, who is a capital importer or exporter, is also not static. Former capital importing countries are also concluding BITs with ISDS when they start exporting capital (e.g. China, India, etc.), even if empirical projects cannot find a correlation between increased investments and the presence of ISDS (the best example is Brazil, which has traditionally shunned ISDS).

Finally, this brings us to the policy question of why we need ISDS to begin with (regardless of its features) when we have robust domestic court systems in place as Arcuri et al. note. This question deserves a discussion on its own, but it may already be pointed out that not all domestic courts in the EU are as robust as that of the Netherlands. Further, even if the new generation FTAs would not preclude direct effect in domestic Courts (which is not the case), at least the CJEU is wary of granting direct effect to international agreements and maintains (despite a suggestion by AG Jääskinen) the general requirement that a provision of an international agreement must have direct effect before it can be invoked to challenge the legality of an internal measure.

It is important to stress that we are not arguing either for or against ISDS, but we do want to point out that the inclusion and reform of ISDS (see the UNCITRAL reform process) is not a black-and-white issue. The recent Economic Partnership Agreement with Japan, proves that the EU is willing to let go of ISDS if a strong trading partner does not wish it to be included in the agreement. Nevertheless, in the case of CETA, both parties to the agreement agreed to the inclusion of ISDS and Canada was also willing to revisit the original agreement so as to include the EU's improved ICS.

3. **The (non-)sense of concluding comprehensive trade agreements as mixed agreements**

In the first point noted above, we did not contest the national parliaments' right to reject (or endorse) CETA but highlighted that they can only do so on very limited issues. That national parliaments have this right is the result of a political choice by the Council not to exercise the EU's shared competences to the fullest. This raises the question what the sense or nonsense is in the decision of the Council to conclude the CETA as a mixed rather than an EU-only agreement.

Indeed, no one contests that the bulk of CETA falls within the scope of the EU's exclusive competence to conduct trade policy. As the CJEU clarified in Opinion 2/15, only a very small part of CETA—the sections on non-direct foreign investment, including the chapter on ISDS—falls outside of the scope of exclusive EU competence and come under shared competence. However, it is not clear whether the Court used the notion of 'shared' competence in the legal sense of Article 4 TFEU or in the more colloquial sense that the EU has partial competences in the field but that the Member States' exclusive competences are also partially in play. Indeed, Kübek & Van Damme highlight that in this regard there are two possible readings of Opinion 2/15, one of which does not qualify ISDS as coming under exclusive Member State competence. In

contrast, Prete argues that ISDS indeed comes under exclusive Member State competence and CETA therefore is a case of obligatory mixity. According to Prete this also follows from *COTIF I* in which the Court clarified that as far as CETA's provisions on portfolio investment goes, they indeed come under EU competence but crucially *COTIF I* lacks a similar clarification for the competence to conclude the ISDS bits of CETA.

Still, President Lenaerts publicly confirmed the shared nature of ISDS in the sense of Article 4 TFEU during a seminar organised by the Belgian Ministry of Foreign Affairs, where he mentioned that "[i]n Opinion 2/15 … the Court decided that competence to enter into an ISDS mechanism is shared between the Union and its Member States" and that"[s]ince there is no qualified majority in the Council to decide that the EU should exercise that competence alone, ISDS mechanisms in recently negotiated trade and investment agreements have to be accepted by the Union and all Member States." Assuming that CETA's ISDS regime indeed falls within the scope of *shared* EU competence, it is worth emphasising, as it implies that recourse to mixity—and thus the involvement of national parliaments to ratify CETA—was a political choice made within the Council, rather than a necessary consequence of the division of competences between the EU and the Member States.

Contrary to what Arcuri e.a. imply, it is not clear-cut that the EU lacks competence to conclude CETA's ISDS chapter, and in contrast it seems that CETA is a case of purely 'facultative mixity'. This only stresses the special responsibility entrusted to national parliaments. Their direct involvement in the ratification of CETA would be merely the result of a political choice on the part of the Council (and not a legal necessity). While they are very much in their right to debate CETA's ISDS regime, they should in our view, in a spirit of sincere cooperation with their colleagues in the EP, confine themselves to that topic. Since the EU, in accordance with its own constitutional requirements, has already given the green light to 95% of CETA over two years ago , a special responsibility rests on the national parliaments when they decide to agree to or reject CETA's ISDS regime.