

The Trans-Pacific Partnership Agreement (TPPA): When Foreign Investors Sue the State

By [Martin Khor](#)

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The investor-state dispute system, whereby foreign investors can sue the host-country government in an international tribunal, is one of the issues being negotiated in the Trans-Pacific Partnership Agreement.

In the public debate surrounding the Trans-Pacific Partnership Agreement (TPPA), an issue that seems to stand out is the investor-state dispute settlement (ISDS) system. It would enable foreign investors of TPPA countries to directly sue the host government in an international tribunal.

In most US free trade agreements (FTAs) with investor-state dispute provisions, the tribunal most mentioned is the International Centre for Settlement of Investment Disputes (ICSID), an arbitration court hosted by the World Bank in Washington.

ISDS would be a powerful system for enforcing the rules of the TPPA, which is currently being negotiated by the US and 11 other Pacific Rim countries. Any foreign investor from TPPA countries can take up a case claiming that the government has not met its relevant TPPA obligations.

If the claim succeeds, the tribunal could award the investor financial compensation for the claimed losses. If the payment is not made, the award can potentially be enforced through the seizure of assets of the government that has been sued, or through tariffs raised on the country's exports.

ISDS is related to relevant parts of the TPPA's investment chapter. One of the provisions is a broad definition of "investment" which includes credit, contracts, intellectual property rights (IPRs), and expectations of future gains and profits. Investors can make claims on losses to these assets.

Under the "national treatment" provision, a foreign investor can claim to be discriminated against if the local is given preference or other advantage.

Under the clause on fair and equitable treatment, which is contained in many existing trade and investment treaties, investors have sued on the ground of non-renewal or change in the terms of a licence or contract and changes in policies or regulations that the investor claims will reduce its future profits.

Finally, investors can sue on the ground of “indirect expropriation”. Tribunals have ruled in favour of investors that claimed losses due to government policies or regulations, such as tighter health and environmental regulations.

The arbitration system has come under heavy criticism, including that the tribunal decisions are arbitrary and can contradict decisions of other tribunals in similar cases.

There is often a situation of conflict of interest. A few lawyers monopolize the international investment arbitration business; they act as lawyers in one case and as arbitrators in other cases. In a few cases, an arbitrator was on the board of directors of the parent company of the investor that took up the case.

There is a pro-investor bias in many cases, with decisions or arguments that are quite clearly unfair to the governments being sued. However, there is no appeal possible.

Another issue is the high awards and the strong enforcement, including seizure of assets. The claims have tended to be very high in recent years, running to billions of US dollars. Awards are usually lower, but recent ones can also be very high, such as the \$2.3 billion award granted by ICSID to an American oil company against Ecuador.

The ability to enforce these awards through seizure of assets owned and located abroad by the government makes ISDS a very powerful instrument.

Other recent investor-state dispute cases include one taken against South Africa by a European mining company claiming losses from the government’s black empowerment programme, and a \$2 billion claim against Indonesia by a UK-based oil company after its contract was cancelled because it was not in line with the law.

Australia has also been sued for billions of dollars by the tobacco company Philip Morris because of its regulation that cigarette boxes cannot promote the logo and brandnames. An American company Renco sued Peru for \$800 million because its contract was not extended after the company’s operations caused massive environmental and health damage.

There are several implications of ISDS under the TPPA. Not conforming to TPPA rules can carry a heavy penalty, since the government can be sued in an international court, and thus governments will be constrained when formulating future policies or implementing existing ones.

It would be difficult for a government to make new policies, as it cannot predict whether certain policies it wishes to introduce or change are allowable, since it is uncertain or unpredictable how a tribunal will view this; the view of a particular tribunal can differ from that of another.

The country’s judicial sovereignty will be affected. Investors will choose to take up cases in the international tribunal where their chances of success and the payout are higher than in local courts.

The country will become vulnerable to multi-million-dollar and billion-dollar legal suits taken by foreign investors. Potentially this may cost the government a lot of financial resources.

The TPPA talks are still going on, and thus the ISDS component can still be negotiated. However, there is probably limited room for negotiation on the key aspects, since the US is

unlikely to deviate from the main points in its existing FTAs.

If ISDS is deemed to pose too many problems, one option is to ask for an exception, i.e., that it does not apply to the country concerned, similar to what Australia has requested. It is, however, doubtful whether such a request will be granted by other TPPA countries.

Martin Khor is Executive Director of the South Centre, an intergovernmental policy think-tank of developing countries, and former Director of the Third World Network.

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