D5 | INVESTMENT TREATIES: HOLDING GOVERNMENTS TO RANSOM

Introduction

As the WHO pushes for the implementation of the Framework Convention on Tobacco Control (FCTC), the tobacco industry has, in the words of outgoing WHO Director General Margaret Chan, "made it absolutely clear that it has no intention of abandoning a business model that depends on enticing millions of new users – especially young people – to its deadly products"[1]. For the multinational tobacco industry, the weapon of choice in thwarting the adoption and implementation of the FCTC has been the use of provisions in investment treaties that allow investors to initiate binding arbitration against governments in international forums.

Nearly all developing countries have signed bilateral investment treaties (BITs) with developed countries. Increasingly, free trade agreements (FTAs) also feature investment protection chapters. There are 3268 treaties with investment protection provisions, of which 2923 are BITs (Reid Smith and Allas Portilo, 2016). BITs were originally aimed at protecting foreign investors from nationalization of their investments. However over time, both the provisions in BITs and their interpretation have expanded the meaning and scope of protections available to investors. Protection to 'investors' is now interpreted to include scrutiny of social, environmental and health policies of sovereign governments. Such policies are now being challenged by foreign investors on the plea that they put their investments at risk. Such challenges can involve the Investor-State Dispute Settlement (ISDS) mechanisms that are embedded in trade and investment treaties.

Understanding investment treaties and ISDS

Investment treaties incorporate provisions which protect investments by private entities from being expropriated by a foreign government. They also grant 'fair and equitable' treatment to foreign investors as is enjoyed by national investors. Such protection often is in conflict with public interest.

These treaties generally have a very broad definition of investment that goes well beyond the commonly understood definition of property, to include intellectual property rights, licences and permits, debt securities and loans and profits and future/expected profits. They also define investors very broadly and in several treaties simply having a branch office is sufficient to recognize a company as an investor. Under the now shelved TPP for instance, the mere act of 'channelling resources or capital in order to set up a business' or 'applying for permits and licences' would have been sufficient to qualify as an investor[2].

'Investors' are then entitled to various protections under these treaties. The first being 'national treatment' which requires that national policies and laws must apply equally to foreign investors as they do to local firms. Further, 'most favoured nation' (MFN) clauses in these agreements require that if a country is party to one investment treaty, it must provide investors covered by other investment treaties with the same protection and privileges as available in the former case.

Investors are also entitled to 'fair and equitable treatment'. There is a wide range of interpretations of 'fair and equitable treatment' which governments have found difficult to comply with. This can be seen in the statistics for disputes under US trade or investment treaties where 74 per cent of the time when investors win, there has been a violation of fair and equitable treatment (FET); for instance tribunals have found that laws or policies that differed from investors' 'reasonable expectations' have amounted to FET violations[3]. Broad interpretations of this provision in tribunal decisions can lead companies to claim reasonable expectations about future profits arising from intellectual property filings. Thus changes to IP laws that impact their expectations of profits could be interpreted as a FET violation.

The third is protection from expropriation without compensation. Typically in these treaties expropriation is only permissible if it is for a public purpose and carried out in a non-discriminatory manner. Further any expropriation requires the prompt payment of adequate and effective compensation, even in cases where expropriation is done for a public purpose. The quantum of compensation is required to be equivalent to the fair market value of the investment before expropriation. Expropriation is traditionally understood to mean nationalization and the taking of physical property but these treaties also protect from 'indirect expropriation'. This has been interpreted to mean reduction in the value of a foreign investment due to regulations and other government actions (Kelsey and Wallach, 2012). Thus, for example, issuing compulsory licences issued by governments to allow production of cheaper generic versions of patented medicines could be interpreted as 'indirect expropriation'.

When investors claim violation of their rights, as laid down in these treaties, they can initiate arbitration proceedings against governments claiming compensation in specialized tribunals. Such tribunals include the World Bank's International Centre for the Settlement of Investment Disputes (ICSID), the UN Commission on International Trade Law (UNCITRAL), the Permanent Court of Arbitration at the Hague or in chambers of commerce. Thus, foreign investors pursue claims against the host country outside the country's judicial system. If they are successful, arbitration tribunals may make awards both in the form of monetary damages, including applicable interest, and/or in the form of property restitution.

The ISDS system enables foreign investors and corporations to directly sue governments. It may be recalled that the BITs or Free Trade agreements (FTAs) themselves are signed between countries. Typically, if there is a dispute over the implementation of these international agreements, the signatories to the agreement – the governments – file disputes against each other. The ISDS mechanism allows investors, who were never signatories to the agreements, to bring disputes against governments. Disputes between governments often may not be pursued or may be settled out of diplomatic considerations. However private businesses face no such diplomatic constraints as evidenced by the cases described below..

Philipp Morris sues Uruguay and Australia

The cases filed by US cigarette manufacturer, Philipp Morris, against Uruguay (Porterfield and Byrnes, 2011) and later Australia (BBC, 2011) illustrate the implications of ISDS for public health. In these disputes, Philipp Morris alleged that tobacco warnings on cigarettes or rules for plain packaging amounted to infringements of their trademarks which are considered to be 'investments'.

The case against Australia[4] originated with the Tobacco Plain Packaging Act, 2011 which required removal of brands from cigarette packs. Under the Hong Kong–Australia BIT, Philip Morris Asia Limited (PMA) initiated arbitration

Image D5.1 Protest against EU Philippines FTA, 26 May2016 (M3M) against Australia for the expropriation of its IP due to this legislation. The IP in question were trademarks held by an Australian subsidiary of PMA. In December 2015, the arbitration tribunal established for this dispute at the Permanent Court of Arbitration (PCA) held that the case could not be heard on a jurisdictional issue; specifically that Philip Morris Asia changed its corporate structure to take advantage of the provisions of the Hong Kong-Australia BIT. It was only in February 2011 that PM Asia acquired all shares of PM Australia and became the direct owner of Philipp Morris's investment in the country. The tribunal held that whether such a restructuring was indeed an abuse depended on whether there was a foreseeable dispute and since by February it was evident that Australia would be introducing plain packaging rules, a dispute was indeed foreseeable.

In Philipp Morris' case against Uruguay[5] in 2010 the claim was brought by two Swiss companies and one Uruguayan company from the Philip Morris Group under the Switzerland-Uruguay BIT. The measures challenged by these companies were Ordinance 514 of August 18, 2008 which required tobacco warnings on cigarette packs and prohibited variants of brands such as *Light*, *Blue* and *Fresh Mint* in the case of Philip Morris. Also challenged was Presidential Decree 287/009 of 15 June, 2009 which increased the size of the warnings from 50 to 80 (Brauch M D 2016). These measures, according to Philip Morris amounted to an expropriation of its investment and a violation of the requirement of fair and equitable treatment among other things.

In July 2016, a tribunal at ICSID dismissed Philip Morris's case, ordered it to bear the entire costs of the arbitration and partially reimburse Uruguay's legal expenses to the tune of US$ 7 million. The tribunal found that trademarks do not confer an absolute right of use which is free of state regulation but only the right to exclude others from using it. They also held that the limitation of space for Philip Morris to display its brand on the cigarette pack to 20 per cent did not substantially deprive the value of their investment and so held that the claims of expropriation were invalid. Rejecting claims of violation of fair and equitable treatment, the tribunal found that Uruguay's actions were based on the WHO's FCTC process which was supported by scientific evidence and were adopted in good faith to protect public health and were not discriminatory or arbitrary.

Pharmaceutical companies in the fray

The tobacco disputes have not been the only ones involving the ISDS mechanisms. The implications of ISDS on access to generic medicines became evident in the dispute between pharmaceutical company Eli Lilly and the Government of Canada filed under the North American Free Trade Agreement (NAFTA). In Canada, Eli Lilly's patents on two drugs – atomoxetine and olanzapine – were revoked on grounds of failure to prove the 'utility' of the patented drug, as required under Canada's patent law. Eli Lilly filed its intention to initiate formal proceedings under NAFTA in 2012 and then filed an arbitration notice in 2013.

Eli Lilly claimed that the patent revocation violated the minimum standard of treatment and fair and equitable treatment guaranteed to foreign investors under NAFTA which obliged signatories to accord to another party "treatment in accordance with international law, including fair and equitable treatment and full protection and security". Eli Lilly further claimed that the patent revocation discriminated against Eli Lilly in favour of generic firms, in violation of Canada's national treatment obligations under NAFTA. Eli Lilly also alleged that the patent revocation amounted to an expropriation of property rights, alleging violation of the WTO TRIPS Agreement, NAFTA's intellectual property rules, the Patent Cooperation Treaty and the Paris Convention for the Protection of Intellectual Property. Eli Lilly demanded a compensation of 500 million Canadian dollars for these violations.

In 2017, the tribunal established under ICSID dismissed all of Eli Lilly's claims against Canada and directed it to pay all of Canada's arbitration costs and 75 per cent of their costs of legal representation and assistance.

Energy and environment sector

Several cases have been filed by investors in a number of countries, both developd and developing, in response to government regulations in the environment and energy sector. Table D5.1 summarizes some of the important cases.

TABLE D5.1: Cases related to investor state disputes in the environment and energy sector

Policy being challenged	Bans on mining due to environmental concerns	Regulations to fight for energy transition and against climate change	Other environmental protection measures
Case	Pacific Rim v. El Salvador	Vattenfall v. Germany I (environmental restrictions on coal)	Methanex v. United States (chemical and groundwater contamination)
	Renco v. Peru	Vattenfall v. Germany II (phasing out nuclear energy)	
	Gabriel Resources v. Romania	Lone Pine Resources v. Canada (fracking moratoria)	
	Infinito Gold v. Costa Rica	Perenco/Burlington v. Ecuador (oil taxes)	Ethyl v. Canada (ban of environmentally damaging gasoline additive)
	Bilcon v. Canada	TransCanada v. United States (cancellation of pipeline due to environmental concerns)	
	Glamis v. United States		

Source: TNI, Friends of the Earth International and CEO, 2017, Winning the debate against pro-ISDS voices: An activist's argumentation guide, https://www.tni.org/files/9837452346812786.pdf

Limited victories

Supporters of ISDS have characterize cases, where tribunals ruled against corporations, as evidence that the ISDS system works and is not arbitrary or stacked in favour of investors. However, experience has shown, that the threat of private international arbitration and the exorbitant compensation awarded to investors has had a chilling effect on government regulations and often governments opt for settlements that favour foreign investors. It is important to note that investment treaties can have different provisions, so success for a government in one investment treatment dispute does not guarantee success in a dispute brought under a different investment treaty. There is also no real system of precedent followed in investment disputes and across the multiple dispute settlement forums. In some cases, the mere filing of a dispute is sufficient to achieve a change in laws and policies.

In January 2017, Ukraine settled a dispute filed by Gilead Sciences Inc. in which Gilead reportedly claimed US$ 800 million in relation to its Hepatitis C drug sofosbuvir. This particular dispute highlights another key concern with the ISDS system, i.e. information about the disputes are at times dependent on both parties consenting to make it public. Information about this dispute has been pieced together from some Ukraine government documents with the actual settlement not being made public. The dispute likely related to the registration of a generic version of sofosbuvir. Gilead objected to this in local courts seeking an injunction based on the fact that the Ukraine has data exclusivity laws that prevent the registration of a subsequent generic for five years after Gilead's version was registered. Gilead obtained registration in mid-2015 and in November 2015, a state registry of medicines listed Grateziano, a generic version of the drug produced by Egyptian owned manufacturer Europharma International.

It needs to be noted that Gilead has specifically excluded the Ukraine from voluntary licences given to Indian companies that would have allowed access to cheaper generic versions of sofosbuvir for the millions of people living with Hepatitis C in the Ukraine. Nor does Gilead have a patent on this drug yet. Even as it challenged the generic registration in the local courts, Gilead initiated an investment dispute under the US-Ukraine BIT. It is unclear what arguments and claims Gilead was relying on. An interagency working group set up by the government of Ukraine recommended settling the dispute and a settlement, which remains secret was reached and approved in January 2017. A public statement issued by the Ministry of Justice implied that a discounted price offered by Gilead was also part of the settlement. The Ministry of Health later announced that it was de-registering the Egyptian company's version to comply with this settlement.

Although Australia and Uruguay eventually won the arbitration cases filed against them, it is of note that several countries received warnings from the tobacco industry of similar actions against them and Costa Rica, for instance, dropped plans to implement tobacco control measures in light of the ISDS cases[6]. Recently, leaked documents revealed by Swiss NGO Public Eye revealed that Novartis threatened Columbia with an investment dispute under the Swiss-Columbian BIT over the government ordered reduction in prices of its drug imatinib (Public Eye, 2017).

The fear of adverse findings and huge awards apart, simply the costs involved in defending an investment arbitration are sufficient for several countries to avoid such disputes. Although Philip Morris and Eli Lilly were ordered to cover 75 per cent of the legal costs of the states they were suing, that still left a substantial amount for the States to pay themselves. In the Philip Morris-Uruguay case, the costs claimed by the parties exceeded the claim of US$ 25 million made by the Philip Morris.

IP safeguard proposals

Several countries have now started considering introducing safeguards in new BITs and FTAs to prevent a repeat of cases described above. For instance, the India-Japan Comprehensive Economic Partnership Agreement (CEPA) contains an investment chapter which includes intellectual property in the definition of investment. Article 92(5) of the investment chapter states that the provisions would not be applicable to compulsory licences issued in accordance with the TRIPS agreement. This, however, means that companies can still challenge compulsory licences by claiming that they violate the TRIPS agreement. This introduces another layer of complexity as under the TRIPS agreement only another government can challenge non-compliance with the TRIPS agreement before the WTO Dispute Settlement Body.

Expanded versions of this exception now appear in recent BITs and FTA negotiations in which the USA is involved. These provisions exempt revocation of patents and compulsory licensing from the definition of expropriation. However it is of note that there is no exemption of these measures from claims of violation of fair and equitable treatment. In the case of the tobacco disputes, an exception to ISDS for tobacco control was agreed in Art 29.5 of the TPP [7].

Not just intellectual property rights

Several public interest groups and academics recommend that intellectual property (IP) be removed entirely from the definition of investments. While this may remedy a serious area of concern, it should be noted that IP is not the only basis of ISDS challenges to health policies. Investment provisions have also been used to challenge Poland's attempts to prevent the privatization of its public health insurance company[8] and the ability of Canada to regulate chemicals that can cause health problems (Public Citizen, 2000).

In addition BITs and investment provisions in FTAs have provisions related to 'market access'. Typically they restrict the ability of governments to impose barriers to free flow of goods and services. Barriers imposed by countries can be tariff barriers (duties on imports for example) or non-tariff barriers (not allowing certain goods into the market on health grounds, for example).The loss of flexibility to impose barriers to market access, can pose problems. Traditionally countries (especially developing countries) have used market access restrictions to promote domestic industry. In areas such as medicine production, this may be a vital tool, as it could allow the development of a local pharmaceutical industry.

While developed countries press for market access in trade and investment agreements, they oppose provisions related to 'performance requirements' (PRs). PRs are conditions imposed on foreign investors and can be used to channelize foreign investments in a manner that supports development of local industry, research, etc. Thus a PR that could help local industry, for example, is the requirement of 'technology transfer'. There is a trend towards barring PRs in trade and investment treaties.

A key concern with including investment provisions in FTAs as opposed to stand alone BITs is the link this creates between trade and investment. Where a developing country finds that the abuse of investor protections in these BITs is significant enough to warrant that they be revoked, they would be unable to revoke investment provisions in an FTA as that would involve the revocation of the entire FTA.

Reform, reject, repeal

It is evident that the rights given to investors in BITs and FTAs can significantly restrict a government's ability to regulate how companies operate

Image D5.2 Demonstration in Europe against the Transatlantic Trade and Investment Partnership (third world health aid) within its national borders. Investment treaties or provisions are increasingly being questioned even as the manner in which these provisions have been used by multinational companies to challenge health, environment and other laws and policies have come to light (Oxfam, 2011).

There are now increasing calls for the rejection or the overhaul of the global investment treaty framework. In South Korea, judges have openly objected to investor-state dispute mechanisms highlighting its impact on the sovereignty of the country and on the judiciary[9]. At the height of the tobacco disputes, Australia declared that the government would no longer sign any trade agreement which include investor-state dispute mechanisms[10]. Eventually they did agree to ISDS in the TPP but after having tobacco excluded from the scope of any disputes. South Africa and Indonesia are withdrawing from existing BITs in favour of domestic investor protection laws while others like India are adding safeguards to their model BITs/FTA investment chapters and requesting renegotiations of existing BITs. The US push for ISDS played a significant role in the 2014 suspension of FTA talks between the USA and EU. The EU is now pushing for a permanent, multilateral investment court to address many of the criticisms of the current system. In early 2017, Canada and the EU made an informal proposal for such a multilateral ISDS mechanism to come within the WTO; a proposal that was rejected by India, Brazil, Japan and Argentina.

Even as states grapple with attempts to reform the global investment treaty framework, UN agencies and experts have expressed grave concern over the interplay between BITs and ISDS with human rights treaties. In June 2015, a joint statement by 10 UN experts and special rapporteurs stated that there was "a legitimate concern that both bilateral and multilateral investment treaties might aggravate the problem of extreme poverty, jeopardize fair and efficient foreign debt renegotiation, and affect the rights of indigenous peoples, minorities, persons with disabilities, older persons, and other persons leaving in vulnerable situations[11]." They made key recommendations calling for transparency and public consultation in current trade and investment agreement negotiations, human rights impact assessments of BITs and FTAs and robust safeguards embedded in current BITS and FTAs to ensure full protection and enjoyment of human rights (Reid Smith, 2015).

In his testimony to the European Parliament in 2016, the UN Independent Expert on the promotion of a democratic and equitable international order was more direct, challenging claims that investors need protection, stating: "It is States, particularly developing States, and their populations that need protection from predatory investors, speculators and transnational corporations, who do not hesitate to engage in frivolous and vexatious litigation, which are extremely expensive and have resulted in awards in the billions of dollars and millions in legal costs.' As he noted, 'the time has come to abolish ISDS…and to ensure that henceforth, trade works for human rights and not against them[12]."

Notes

1 See speech by Margaret Chan 'Every tobacco death is an avoidable tragedy. The epidemic must stop here': http://www.who.int/mediacentre/commentaries/early-tobacco-death/en/

2 See TPP text available at website of Analysis and Policy Observatory: http://apo.org.au/system/files/58399/apo-nid58399-98391.pdf Chapter 9, P. 4

3 See note by Public Citizen on this issue: http://www.citizen.org/documents/MST-Memo.pdf

4 Morris Asia Limited v. The Commonwealth of Australia, PCA Case No. 2012-12 http://www.italaw.com/sites/default/files/case-documents/italaw7303_0.pdf

5 Philip Morris Brands Sàrl, Philip Morris Products S.A. and Abal Hermanos S.A. v. Oriental Republic of Uruguay, ICSID Case No. ARB/10/7http://www.italaw.com/sites/default/files/case-documents/italaw7417.pdf

6 See: ' Tobacco Companies Bully Countries: https://sites.psu.edu/stopthetobaccoindustry/tobacco-companies-bully-people-into-purchasing-their-products/

7 See TPP Text here: https://www.tpp.mfat.govt.nz/text

8 Marinn Carlson (Partner) and Peter Kasperowicz, Sidley Austin LL,Dutch insurer Eureko, Polish government settle investment dispute, setting up IPO for Poland's state-owned insurer, available at http://arbitration.practicallaw.com/6-500-6640

8 See: 'Judges debate KORUS FTA task force', The Hankyoreh, 3 December 2011.

10 Public Statement on the International Investment Regime, 31 August 2010 available at http://www.osgoode.yorku.ca/public-statement/documents/Public%20Statement%20%28June%202011%29.pdf

11 See: http://www.ohchr.org/EN/NewsEvents/Pages/DisplayNews.aspx?NewsID=16031

12 See" ' Investor-State dispute settlement undermines rule of law and democracy, UN expert tells Council of Europe'http://www.ohchr.org/EN/NewsEvents/Pages/DisplayNews.aspx?NewsID=19839&LangID=E#sthash.TkSKjpD6.dpuf

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