

## Policy pointers

**There is a strong case** for the UK to review its policy on investment treaties to ensure it can negotiate most effectively with trading partners in a post-Brexit context.

**The stakes are high:** ill-designed treaties could leave the UK government excessively exposed to legal claims by foreign companies, or could fail to address the economic, social and environmental challenges facing the UK today.

**Key areas to consider** would be: a method for conducting a cost-benefit analysis of proposed future treaties; options for formulating them; and arrangements for public consultations.

**A review could develop** a new template for future treaties, and devise an action plan to bring old treaties in line with the new policy.

# Beyond trade deals: charting a post-Brexit course for UK investment treaties

The Brexit referendum has raised questions about the future terms of the United Kingdom's engagement with the world economy. While a debate over the UK's future approach to trade deals has already begun, a similar discussion has yet to develop on the treaties that govern foreign investment. The stakes are high: ill-designed treaties could leave the UK excessively exposed to legal claims by foreign companies and could fail to address economic, social and environmental challenges. While meaningful negotiations are unlikely to start until the new relationship between the UK and the EU has been clarified, now would be a good time for a policy review to define a new approach. The government, parliament and the public have an important role to play in positioning the UK as a global innovator in investment treaty policy.

## Why look at the United Kingdom's future investment treaty policy?

The United Kingdom has played an important role in the historical development of international investment treaties. Such treaties are mostly bilateral, but they also increasingly form part of wider regional trade treaties that contain an investment chapter. These treaties aim to promote investment flows by establishing rules that govern how states must protect and possibly admit investments by nationals of the counterparty state(s) within their own territory. Most investment treaties also allow investors to bring disputes with the host state to international arbitration.

From the first investment treaty the UK signed with Egypt in 1975, to the most recent (Colombia in 2010), the UK has concluded

agreements with over 100 countries, most of which are now in force. But the European Union Lisbon Treaty, which came into effect in December 2009, shifted the power to conclude investment treaties from member states to the EU. With that authority, the EU has conducted major trade and investment treaty negotiations, including for the Comprehensive Economic and Trade Agreement (CETA) with Canada and the proposed Transatlantic Trade and Investment Partnership (TTIP) with the United States.

Given the outcome of the Brexit referendum, the power to conduct investment treaty negotiations — like the power to make trade agreements — is now set to return to the UK government. Politicians, journalists, researchers and activists have started to discuss options for the UK's future trade policy — including whether, when and with which countries to

strike new trade deals. But there has been little debate about future UK investment treaty policy. There are five reasons why investment treaty policy deserves more attention:

## *The treaties the EU has negotiated in recent years have significantly departed from the standard agreements once concluded by the UK*

1. Foreign investment plays an important role in the UK economy.

Estimates suggest that there is more than £1 trillion in foreign direct investment (FDI) in the UK, and UK firms overseas hold an even higher amount of FDI.<sup>1</sup>

2. Investment treaties feature prominently in international economic negotiations. This is clear from the recent or ongoing negotiations of 'trade' agreements such as TTIP, CETA and the Trans-Pacific Partnership (TPP), all of which include substantial investment chapters equivalent to a standalone investment treaty. Some of the countries the UK has identified as possible partners for trade deals do not have an investment treaty with the UK (eg the US and Australia). It is therefore possible that investment policy will form part of any trade negotiations with these countries.

3. Unlike traditional deals concerning tariffs on cross-border trade in goods, investment treaties deal primarily with 'behind-border' measures affecting foreign-owned firms and assets. These include laws, regulations, court judgments and measures adopted by any level of government (local or national). They can cover almost any area of public policy, including industrial strategy, tax, subsidies, healthcare, environmental protection and labour rights.

4. Investment treaties have recently come under intense public scrutiny. With their rules on protection of foreign investment and their provisions allowing companies to sue governments before international tribunals, these treaties have magnified wider concerns about the balance between corporate and public interests. Recent arbitrations initiated under investment treaties include a US company contesting a ban on fracking in Canada; a Swedish company's case against Germany for phasing out nuclear power; a suit against the US government over its decision not to permit construction of a controversial oil pipeline; and a tobacco company's suits against governments for anti-smoking regulations.<sup>2</sup> As the arbitrations have increased in both their number and scope, public concern about investment treaties has intensified.

5. There is now a widespread recognition of the need for countries to ensure coherence between their trade and investment policies and their social and environmental commitments — including under the 2015 Paris Agreement on climate change and the Sustainable Development Goals.<sup>3</sup> The UK investment treaties were concluded before this international agenda crystallised. Debating the treaties can help ensure they advance that agenda.

### **The international investment treaty landscape — a fast-evolving context**

Competence for negotiating investment treaties shifted to the EU in 2009, when the Lisbon Treaty came into effect.<sup>4</sup> In this relatively short timespan, the European and international investment treaty landscape has changed considerably — both with regards to the content of the treaties and the process through which they are made.

Once a largely technocratic process, treaty negotiations can now involve significant public mobilisation. The European Parliament has leveraged its greater say in economic treaty ratification to provide clearer guidance on investment treaty policy and individual treaty negotiations.<sup>5</sup> There has also been extensive citizen engagement. Following activist-led campaigns, the European Commission organised a carefully circumscribed public consultation on the investment chapter of the TTIP. The response rate was 'unprecedented' — involving roughly 150,000 submissions, over 50,000 of which were from the UK, and revealing 'widespread opposition to investor-state dispute settlement in TTIP or in general'.<sup>6</sup> The treaties have also generated lively debate outside the formal consultation.

Partly as a result of this greater scrutiny, the treaties the EU has negotiated in recent years have significantly departed from the standard agreements once concluded by the UK and other EU members. In particular, they have adopted new formulations to reduce the scope for companies to challenge public-interest decisions, though it is as yet unclear how tribunals will apply the revised standards.

The EU has also moved away from the model of private commercial arbitration traditionally used in treaties concluded by the UK and others to embrace a new 'investment court system', which is included in the CETA. This new approach has yet to resolve some fundamental issues in investor-state dispute settlement and has so far failed to quell

the most vocal criticism of the investment treaty regime. Nevertheless, the model does include reforms in terms of the way arbitrators are selected and how conflicts of interest are tackled. It also establishes an appeal mechanism.

Beyond the EU, changing perceptions about the costs and benefits of investment treaties have led several other governments to rethink their policies. As a result, some recent treaties depart considerably from traditional formulations. Agreements and models adopted by countries such as Australia, Canada and India, and at the regional level by the Southern African Development Community, have sought to include more specific formulations for investment protection standards; clauses calling on investors to apply responsible business practices; or more explicit provisions affirming the right of states to regulate in the public interest. Some states, such as Brazil, have concluded agreements that look very different from conventional investment treaties — excluding investor-state arbitration and placing greater emphasis on investment facilitation.

### The need for a new UK investment treaty policy

In this changing context, it would not be realistic or advisable to simply revert back to pre-2009 UK investment treaty practice. There is a strong case for the UK to review its policy, paying particular attention to these three interlinked issues:

**Assessing the costs and benefits of investment treaties.** The policy review would provide a space to identify criteria for decisions regarding whether to negotiate an investment treaty, including robust methods for prior cost-benefit analysis. Potential benefits might include greater inward and outward foreign investment, while potential costs might include exposure to arbitration risks, related liabilities and the impact these may have on public policy.<sup>7</sup>

In debates about the TTIP, it was often claimed that the UK would have little to fear from investor-state arbitration. The UK has concluded many investment treaties, but only on one occasion has it been taken before an investor-state tribunal based on such a treaty.<sup>8</sup> However, the majority of the UK's existing investment treaties are with countries that have small or negligible foreign investment stocks in the UK, including many low- and middle-income countries. Although these investment treaties are formally reciprocal, the investment

flows they cover are largely one-way, which in effect means that the treaties have primarily served to protect UK investments overseas.

Past experience under those treaties is therefore not an accurate predictor of the future. Although opportunities for foreign investors to bring arbitration claims against the UK have so far been limited, this could change in future negotiations with high-income countries that have significant foreign investment stocks in the UK, such as the US. Such treaties may have very different cost-benefit implications, which the UK would need to weigh.

### Considering options for treaty formulation.

The UK would also need to consider what kinds of new investment treaties would best serve its interests. Considering the UK as an investment destination, the policy review would need to explore how future treaties could, for example, promote inward investment while limiting undue exposure to arbitration claims.

At the same time, the review would need to take into account the UK's role as the home state of multinational companies operating abroad, and as a major developed country committed to advancing global sustainable development. Questions include: how to calibrate appropriate levels of protection for UK businesses overseas without unduly affecting policy space in partner countries; how to formulate investment treaties so they ensure that foreign investment provides sustainable benefits in host and home countries; how to devise clauses that promote adherence with international human rights law and international standards of responsible investment; and how to design treaty provisions that help prevent countries from unsustainably lowering labour standards, environmental protection and tax rates to compete for increasingly mobile capital.

A policy review may pave the way for the development of a new treaty template as a basis for future negotiations. It could also allow for a review of the UK's existing stock of investment treaties, some of which date to the 1970s (eg Egypt, South Korea, Indonesia, Thailand) and the 1980s (eg Cameroon, China, Philippines). India — touted as a possible key partner in future trade negotiations — has an investment treaty with the UK dating back to 1994. By sticking to these old treaties, the UK may miss an opportunity to harness evolving international economic law to meet the complex economic, social and environmental challenges facing it and its partners today.

**Developing arrangements for public consultation.** A policy review would provide an opportunity for the UK to clarify the decision-making process on investment treaties. Extensive citizen engagement on investment policy issues over the past few years suggests new consultative arrangements are needed. This may involve a greater parliamentary role in setting policy and overseeing negotiations, and new approaches to stakeholder consultation at both the policymaking and treaty negotiation stages.

## Conclusion

As a major economy, the UK is set to play a prominent role in international economic

governance. It is important that investment policy choices are properly analysed and debated. A policy review would provide an opportunity for the UK to do this and update its investment treaty practice. The result will be a more effective and widely supported strategy that will help the UK to address the economic, social and environmental challenges it faces today.

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## Knowledge Products

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## Notes

<sup>1</sup> United Nations Conference on Trade and Development (UNCTAD) (2016) World Investment Report. <http://unctad.org/en/Pages/DIAE/World%20Investment%20Report/Annex-Tables.aspx>; Dhingra, S *et al.* (2016) The impact of Brexit on foreign investment in the UK. *Brexit Analysis* (3). Centre for Economic Performance, the London School of Economics. <http://cep.lse.ac.uk/pubs/download/brexit03.pdf> / <sup>2</sup> The cases are Lone Pine Resources Inc. v. The Government of Canada, ICSID Case No. UNCT/15/2 (ongoing); Vattenfall AB, Vattenfall Europe AG, Vattenfall Europe Generation AG v. Federal Republic of Germany, ICSID Case No. ARB/09/6 (ongoing); and TransCanada Corporation and TransCanada PipeLines Limited v. The United States of America (ongoing). Different Philip Morris affiliates brought arbitrations to challenge Australia's and Uruguay's tobacco control measures. Several years after it was initiated, the case against Australia was dismissed on jurisdictional grounds: Philip Morris Asia Ltd v. Australia, PCA Case No. 2012-12, Award on Jurisdiction and Admissibility (17 December 2015). The case against Uruguay proceeded to the merits. Two out of the three arbitrators rejected the claims against Uruguay, but the third arbitrator would have found Uruguay in breach of the investment treaty. Philip Morris Brands Sàrl v. Uruguay, ICSID Case No. ARB/10/7, Award (8 July 2016). See also Voon, T and Mitchell, AD (12 September 2016) Philip Morris v. tobacco control: two wins for public health, but uncertainty remains. *Columbia FDI Perspectives* (182). <http://ccsi.columbia.edu/files/2013/10/No-182-Voon-and-Mitchell-FINAL.pdf> / <sup>3</sup> Paris COP Decision & Paris Agreement art. 14. (12 December 2015) UN Doc. FCCC/CP/2015/L.9/Rev.1. <https://unfccc.int/resource/docs/2015/cop21/eng/I09.pdf>; United Nations Department of Economic and Social Affairs. Sustainable Development Knowledge Platform. Transforming our world: the 2030 Agenda for Sustainable Development, A/RES/70/1 (21 October 2015). <https://sustainabledevelopment.un.org/post2015/transformingourworld> / <sup>4</sup> Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community (3 December 2007), Brussels. / <sup>5</sup> See for example European Parliament Resolution on the future European international investment policy (6 April 2011) (2010/2203(INI)). [www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2011-0141+0+DOC+XML+V0//EN](http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2011-0141+0+DOC+XML+V0//EN); European Parliament Resolution on the EU-China negotiations for a bilateral investment agreement (9 October 2013) (2013/2674(RSP)). [www.europarl.europa.eu/sides/getDoc.do?type=TA&language=EN&referencce=P7-TA-2013-411](http://www.europarl.europa.eu/sides/getDoc.do?type=TA&language=EN&referencce=P7-TA-2013-411) / <sup>6</sup> European Commission (2015) Online public consultation on investment protection and investor-to-state dispute settlement (ISDS) in the Transatlantic Trade and Investment Partnership Agreement. [http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc\\_153044.pdf](http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_153044.pdf) (p.14). / <sup>7</sup> For an example of how the UK could conduct a cost-benefit analysis, see Poulsen, L *et al.* (2013) Report to the Department for Business Innovation and Skills. Costs and benefits of an EU-USA investment protection treaty. [www.italaw.com/sites/default/files/archive/costs-and-benefits-of-an-eu-usa-investment-protection-treaty.pdf](http://www.italaw.com/sites/default/files/archive/costs-and-benefits-of-an-eu-usa-investment-protection-treaty.pdf); evidence on whether investment treaties do promote foreign investment is inconclusive; see for example Sauvart, KP and Sachs, L (eds) (2009) *The effect of treaties on foreign direct investment: Bilateral investment treaties, double taxation treaties, and investment flows*. Oxford University Press; Yackee, JW (2011) Do bilateral investment treaties promote foreign direct investment? Some hints from alternative evidence. *Virginia Journal of International Law* 51(2) 397–442. / <sup>8</sup> Webb, D (2015) Standard Note on the TTIP. [www.parliament.uk/briefing-papers/SN06688/the-transatlantic-trade-and-investment-partnership-ttip](http://www.parliament.uk/briefing-papers/SN06688/the-transatlantic-trade-and-investment-partnership-ttip)