A CONCEPT PAPER:
THE TIME FOR INVESTOR STATE MEDIATION HAS COME

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In 2017 Malik Dahlan and I wrote an article[i] on the need for investor state mediation, in light of the criticism that the investor state dispute system (ISDS) faced from many quarters. We postulated the following:

> *This paper argues that the current criticisms of Investor-State Dispute Settlement („ISDS") are ill-informed and attempts at reforming the system are misguided. The definition of ISDS itself has been, for a long time, limited to investment quasi-judicial bodies or at best arbitration. Analysis of the roots of the ever growing backlash reveals that the main causes for concern are politically negotiated investment treaties, an inherently biased system, lack of transparency, and inconsistent decision-making. Examination of the core reasons behind these complaints leads to the conclusion that the EU Commission's solution to reform ISDS through a permanent court raises more issues and will throw ISDS into disarray. A better approach is to accept the premise that the current system needs improvement. However, accepting this premise requires regulating disputes themselves, rather than simply regulating the resolution of cases, and establishing standards when unable to regulate these. The regulation of disputes would allow the work already begun by UNCITRAL through its notes on transparency to continue. This study will review how introducing mediation to regulate the process of Investor State Disputes ("ISD") can improve and indeed complement the procedural gap evident in the current ISDS system. In particular, while considering more recent investment regimes, it will use the current effort by the Energy Charter Treaty Secretariat to facilitate mediation within the Treaty as an example of how this can be done.*

The World is now a different place from that of 2017. It has witnessed global supply chains being broken, energy market collapse, with extremely limited travel and transportation being possible, with industries closed, mass unemployment, legal obligations in disarray and international trade at a standstill.

The effect of COVID-19 hindering global cooperation is in fact to accelerate a situation that had already begun as far back as the 2008 financial crisis. This started the scramble by States to begin the process of looking, in that case at international finance and the institutions behind it, with great suspicion. The drive for Foreign Direct Investment (FDI) and all the benefits it could bring a State, began to be countered with the exposure that States faced if not only an investment, but the whole financial system supporting the global trade system, began to go wrong. This sentiment was further enhanced by the election of Donald Trump and his rampant nationalism and questioning of the post-World War II international order and it's Bretton Woods institutions. A trade war with China, necessary or unnecessary, added to the reversal of international trade trends. Suddenly multi-national companies faced tensions if they were seen to be making foreign investments, at the expense of employees in their own home country or Region. What is more concerning, is the challenges to a conceptional phenomenon "international supply chains" disruption and reshoring, a concept that will change dramatically how global trade investment will be governed.

The International Monetary Fund (IMF) estimates that almost three-quarters of the increase in trade between 1993 and 2013 was due to the growth of **supply chains.** With trade rising fivefold in those 20 years, the supply chains helped power global economic expansion. As significantly, they were an important source of disinflation. Before Covid-19 hit, the Bank for International Settlements estimated that global inflation would have been about one percentage point higher were it not for the supply-chain enabled efficiencies of global production. As part of a growing backlash against globalization in general, and China in particular, nations are threatening to bring their offshore investments back home.

Yes globalization was criticized for exploiting workers in developing countries, for accelerating the rate of climate change, for increasing discrepancies between rich and poor within countries, for allowing the West to maintain its dominance in technological innovation and know how, while sending low cost jobs to developing countries. All of this has credence, but globalization has without doubt provided more jobs, higher incomes, better education, better health and perhaps better governance to large portions of the World, where the picture was very different 70 years ago. One must also ask, what the alternative would have been if this had not occurred after the devastation brought by World War II.

What will this new trend mean for globalization and international trade in the post Covid-19 world and what will the impact be on ISDS? Perhaps more to the point of this Paper, will the current pushback on globalization and its institutions provide a catalyst for the development of investor-State mediation.

With the signing of the United Nations Convention on International Settlement Agreements Resulting from Mediation (the "Singapore Convention on Mediation") in Singapore in August 2019, mediation has been given new credibility as an international process for the resolution of disputes. To understand that in the context of investor State disputes one must first look at what has been happening in the way of encouraging the use of mediation generally as a tool of international relations and diplomacy. In the past, mediation simply was not often contemplated

in the context of investor state disputes settlement (ISDS). It had its own unique dispute resolution system that had grown out of Investment Treaties negotiated between individual States (bilateral investment treaties or BITS) or on a multi-lateral basis between larger groups international organization of States such as NAFTA. Previously, these agreements contemplated that *international arbitration* would be used to finally resolve disputes between investors and states. *International mediation* was not even mentioned or contemplated to have a role in these disputes. ICSID, the body of the World Bank responsible for trade disputes had arbitration rules and in addition, a set of conciliation rules. The conciliation rules were not however, a form of mediation, but rather a tribunal that heard the dispute and then rendered a non-binding opinion. Most parties never used conciliation and moved directly to arbitration. The cooling off period provided for in BITs (usually 3 to 6 months) was not used to try to find a resolution to the dispute, but rather to prepare for the arbitration.

Five years ago, we started our efforts in the critical energy apace by assisting the Energy Charter Treaty (ECT) Secretariat, a grouping of 54 States which establishes a multilateral framework for cross-border cooperation in the energy sector, look at how mediation could be introduced to its Rules. The Rules provided for arbitration to resolve disputes with investors and had a reference to conciliation, without any specific process. The Secretariat was interested in filling in the gaps by providing for the possibility of mediation. We worked on a mediation guide, which would provide the member States with an outline of the mediation process and how it might be used in investor state disputes. The Guide on Investment Mediation was published on the 19th of July 2016. It was recognized that the Guide alone was not enough. States have largely not mediated, because of the lack of an internal framework, through which the mediation process could be carried out. Issues such as authority to settle, transparency vs confidentiality, responsibility, liability for taking decisions, and state budgets were all a factor. As a result, The Secretariat then went on to review with the member States a model framework that could be adopted within state structures, through which these issues could be dealt with. This Model Instrument on Management of Investment Disputes was published on the 23rd of December 2018 and has been adopted in the interim by several Member States.

In addition to the ECT, we have also been working with International Mediation Institute of The Hauge (IMI), International Centre for Settlement of Investment Disputes (ICSID) and the Centre for Effective Dispute Resolution (CEDR) to develop IS mediation awareness programs and training for mediators and States. It was recognized that without this training the knowledge required for States to mediate these disputes, would not exist. In addition, to give the process credibility a cadre of mediators, who not only understood mediation, but also ISDS had to be trained. Since 2017, several annual IS mediator training courses have been held and mediators capable of handling these cases are now prepared.

Even more important for the acceptance of mediation in these disputes is the fact that ICSID, the organization through which most of these disputes are heard, has given its full support to the development effort. This culminated with ICSID publishing its own IS mediation rules. This has given the initiative credibility with both investors, their counsel and States and was a strong step forward to making mediation part of the ISDS process.

In fact, there have already been several important investor state disputes where mediation has now been used. The most recent reported case (as many are not reported), was that of the Dominican Republic and Oldebrecht that was mediated this January by well-known international mediator Mrs. Mercedes Tarrazón. The matter was mediated under the ICC mediation rules and led to a settlement agreement between the parties.

To understand the significance of ISDS mediation, on the development of investor-State mediation one need only look at the Preamble of the Singapore Convention. It states:

> ***Recognizing*** **the value for international trade of mediation as a method for settling commercial disputes in which the parties in dispute request a third person or persons to assist them in their attempt to settle the dispute amicably,**
>
> ***Noting*** **that mediation is increasingly used in international and domestic commercial practice as an alternative to litigation,**
>
> ***Considering*** **that the use of mediation results in significant benefits, such as reducing the instances where a dispute leads to the termination of a commercial relationship, facilitating the administration of international transactions by commercial parties and producing savings in the administration of justice by States,**
>
> ***Convinced*** **that the establishment of a framework for international settlement agreements resulting from mediation that is acceptable to States with different legal, social and economic systems would contribute to the development of harmonious international economic relations,**

States by signing and ratifying the Convention have recognized the use of mediation as a legitimate public policy instrument for resolving cross border disputes. This gives mediation legal credibility and certainty as a dispute resolution mechanism that can be used as part of the dispute resolution toolkit. Once States have acknowledged this for commercial disputes generally, it is difficult for them to take the position that it does not apply to the State itself or it's agencies when dealing with investors.

If we take the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, as an example, very few States have excluded the application of the Convention to arbitrations involving States or their agencies. In fact, one of the reasons international arbitration became popular and an acceptable dispute resolution tool, was that arbitral awards can also be enforced against States under the New York Convention. This example provides the blueprint for the enforcement of mediated settlements against States as well. It is not so much enforcement that is important, as most States when they actually agree to a Settlement will abide by its terms, but the recognition by States through the Singapore Convention that mediation is an acceptable means of resolving disputes.

Given the unprecedented crises the world is currently facing, the imperative to employ mediation in an investor State context has only grown. Arbitration, as a mechanism for resolving these disputes has limitations. Some recent developments help to emphasis this further. The Columbia

Center on Sustainable Investment has called for a moratorium on all arbitration claims by private corporations against governments using international investment treaties. On the 5th of May 2020, a large number of EU Member States signed an agreement for the termination of Intra-EU bilateral investment treaties. This implements the March 2018 European Court of Justice judgement (*Achmea* Case), where the Court found that Investor-State arbitration clauses in intra-EU bilateral investment treaties are incompatible with the EU Treaties.

In December of last year, a Colloquium called for by Harvard University, brought together key stakeholders in the IS mediation international community with negotiation scholars to Harvard to define the obstacles to mediating investor-State disputes and put forth a path for potential options to overcome them. The Colloquium also resulted in the establishment of a Working Group and newly published Report set a path to move the process forward. Key insights set out in the Report are:

- It is important to view mediation as *assisted negotiation*. Losing sight of this can cause misunderstandings about what mediation is trying to accomplish, and what its place should be in the ISDS system. The need for 'assistance' in negotiations creates a desire on both sides to obtain help, voluntarily, from a *neutral* party. Identifying this neutral party in various scenarios is one of the major challenges facing mediation processes within ISDS.
- Careful mapping of stakeholders and their interests in each type of dispute can enable us to identify areas of common ground, as well as helping to find linkages to parties outside of the central dispute that could act as a bridge between the main conflicting parties.
- Transparency as a goal in ISDS creates certain problems. While desirable from a normative perspective, it can hinder efforts at mediation by exposing early stages of discussions to public scrutiny, thereby creating pressure that can lead to posturing and unproductive dialogue.
- There is also a clear benefit to political actors in relying on processes that are legally binding (as in arbitration). Political actors may prefer to engage in a formalized dispute with a designated arbitrator because even where the outcome is not in their favor, they can shift the blame for said outcome onto the 'higher powers' that made the ruling. By contrast, they are more directly responsible for the outcome of any agreement reached via mediation between the two parties. So, there is potentially a lack of incentive for governments to adopt and political actors to enter into mediation processes.
- For companies that are multifaceted and conduct a variety of types of business in different countries, bringing a formal arbitration claim can be counter-productive. For these types of businesses, it may be more prudent to accept even egregious violations by host states because a public confrontation with the government is likely to lead to negative repercussions in their future transactions with this state. In some ways, then, companies can face pressure to accept a state's infringements upon formal arrangements in the current ISDS system.
- There are two major obstacles to the more effective implementation of mediation in ISDS: (1) a lack of awareness of mediation as an alternative to arbitration, and (2) the lack of a formal, legal framework to support mediation and mediated settlements.

- A potential challenge to wider implementation of mediation in ISDS is the divergence in *rule by law* vs. *rule of law* from state to state. Mechanisms that are put in place to institutionalize mediation as a viable alternative must be sensitive to differences in the way that power is distributed (and decisions are made) in various cultures.
- There are three primary approaches to dispute resolution: (1) Power-based (e.g. labor strikes), (2) Rights-based (e.g. courts, arbitration), and (3) Interest-based (this is where mediation can be most effective: by appealing to the sides' interest in finding a mutually beneficial resolution).
- The idea of "mediation" perhaps needs to be framed in a different manner. The term "mediation" can evoke a sense of a formalized system of dispute resolution that may bring in the confrontational aspects of arbitration and legal proceedings. The challenge lies in creating informal systems that can take effect *prior* to the crystallization of a more formal dispute. The ideal *timing* of mediation along the timeline of a conflict's development is thus a central question.
- A significant challenge of our time is the growing rhetoric, particularly in politics, that the "system" writ large (ISDS included) is corrupt. This is likely to taint any alternative systems that are proposed, including mediation. We must therefore consider how to reverse this rhetorical trend and regain the trust that is necessary to legitimize any dispute settlement or mediation system.
- While the conventional wisdom is that law firms are opposed to mediation, in recent years several international firms have developed models to make a profit from mediated settlements. Lawyers may not be the obstacle they were once perceived to be.

A follow-up Forum on IS Mediation will be held at the British Institute for International and Comparative Law (BIICL) this Autumn, which recently published a report on the urgent need for "Breathing Space" for disputes arising out of international commercial activity. The forum will focus on working with States to ensure appropriate frameworks exist to permit mediation to take place.

All this activity is very timely given that Foreign Direct Investment (FDI) is already taking a big hit as a result of COVID-19 and global trade retrenching and will most certainly get worse. States now have to do all that is possible to create a friendly investment climate. One key element is having a perceived transparent and fair system for resolving investor disputes. Clearly, early dispute resolution, rather than arbitration will play a role in this. Some States have already implemented ombudsperson programs and in addition, have a stated policy of mediating disputes as a prerequisite to arbitration. In essence, this is much in line with our premise that disputes have to be regulated, meaning that there is a process in place that gives scope for resolution through various steps along the way.

COVID-19 has created a situation in which many investment agreements will not be able to be performed strictly in accordance with their terms. This could be on the investor's part, but also on the part of the State, which suddenly has seen its budgetary commitments dramatically altered. Tellingly, the Colombia Initiative's call for a moratorium addresses this particular issue head on.[ii]

This will not be the only call for such suspensions of ISDS, as States struggle to realign many types of commitments due to budget constraints. This is precisely where mediation can play a vital role, in helping the investor and the State to restructure their respective legal commitments and in many cases permit the investment to continue in a different form or bring it to an end on agreed terms. Arbitration cannot provide these remedies and in any event enforcing an arbitral award against a State that cannot or seeks to avoid payment because of the Crisis, hardly makes good business sense.

The narrative is clear. States now have to do all that is possible to create a climate of investment facilitation and compromise. One key element is having a perceived transparent, compromise oriented, and fair system for resolving investor tensions and disputes. Clearly, early dispute avoidance and regulation, rather than adversarial engagement will play a role in this. The time for mediation to become an integral tool of investor State dispute resolution is now.

Our Concept Proposal is therefore the following:

1. That States seeking to attract FDI implement an internal framework for permitting mediation along the lines of the ECT Model Instrument;

2. That training in mediation awareness be implemented so that key officials are familiar with the mediation process and their own internal framework;

3. That States adopt a regulated approach to dispute resolution with investors, permitting for structured negotiation through a neutral, such as an ombudsperson;

4. Given that ICSID is now promulgating its mediation rules, that mediation become a prerequisite, before arbitration can be commenced in ISDS matters, or at least implemented in parallel to arbitration proceedings;

5. That even where a dispute is arbitrated through to award, that mediation be available, if needed, to provide a framework for implementation of the award.

[i] INVESTOR-STATE DISPUTE SETTLEMENT RECONCEPTIONALIZED: *REGULATION OF DISPUTES, STANDARDS AND MEDIATION* M. R. Dahlan, *Professor of International Law and Public Policy,* Queen Mary University of London Wolf von Kumberg, Registrar of the International Dispute Registry. Vol. 18: 467, 2017] *Investor-State Dispute Settlement Reconceptualized* PEPPERDINE DISPUTE RESOLUTION LAW JOURNAL

[ii] **a** PERMANENT RESTRICTION **on all arbitration claims related to government measures targeting health, economic, and social dimensions of the pandemic and its effects. These investor-state cases (often referred to as "ISDS" cases) empower foreign private companies to challenge government actions that affect narrow**

corporate interests, and often result in large payouts, sometimes of billions of dollars, to these companies for alleged lost profits. These suits pose an immediate danger to the ability of developing nations, and the global community as a whole, to confront the COVID-19 challenge.