# SUBMISSION TO THE AUSTRALIAN GOVERNMENT DEPARTMENT OF FOREIGN AFFAIRS AND TRADE REVIEW OF AUSTRALIA'S BILATERAL INVESTMENT TREATIES

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***Executive summary***

*This submission proposes terminating Australia's older-style BITs or renegotiating and replacing them with new agreements that contain safeguards, including the exclusion of investor-state dispute settlement, that will protect the Australian government's capacity to regulate or take measures to address climate change and its effects.*

## 1. Introduction

This submission addresses the following questions proposed for consideration by the August 2020 Discussion Paper published by DFAT ('the Discussion Paper'):

- Do you have concerns about Australia's existing BITs? If so, please comment on any specific provisions of concern.
- If Australia took the approach of re-negotiating at least some of the existing BITs, do you have views on which clauses should be included in a renegotiated agreement?
- In your view, does the existence of a BIT impact on the flow of foreign direct investment and/or portfolio investment? Please comment, if possible, both generally and with reference to specific existing BITs.

## 2. Concerns about Australia's existing BITs

As observed by the Discussion Paper, the BITs to which Australia is currently a party, which came into force between 1988 and 2009, 'contain relatively broadly drafted provisions and do not contain the explicit safeguards generally included in more modern treaties'. As the Philip Morris plain packaging dispute demonstrated, this leaves legitimate regulatory measures taken by the Australian government open to challenge by investors. Even if Australia would win all of any such claims, they are nevertheless expensive to defend. Defeating the Philip Morris claim, for example, cost Australia AU$24 million, not all of which was recoverable.[1] Additionally, Australian cannot take for granted that it will keep winning such cases in light of the unpredictability of tribunals and the suspicion they have at times shown towards state regulatory measures.

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[1] *Philip Morris Asia Limited v The Commonwealth of Australia*, PCA Case No 2012-12 (Final Award Regarding Costs, 8 July 2017).

While the Discussion Paper acknowledges that Australia's modern Free Trade Agreement (FTA) practice seeks to protect against investors challenging public health measures, this submission proposes that the same be done in respect of measures relating to climate change. Such measures could be defined to include measures taken to, for example, further the objectives set out in Article 2 of the Paris Agreement,[2] transition to renewable energy or achieve net zero greenhouse gas emissions.

There are a multitude of reasons that dictate particular emphasis on climate change when it comes to Australia's BIT policy. The first reason is that unlike in other policy areas, there is overwhelming scientific consensus in regards to the existence of climate change, its anthropogenic character, and the fact that radically reducing and eventually eliminating greenhouse gas emissions is necessary for any solution. Australia relied heavily on overwhelming scientific consensus in regards to the negative effects of smoking and the benefits of plain packaging in its prolonged multi-forum litigation against Philip Morris. Therefore, it would be consistent to do so in regard to climate change as well. Additionally, the gravity and urgency of climate change mean that even short delays owing to ongoing investment litigation and/or concerns about the possibility of such litigation will have important — even irreversible — negative effects.

The threat of investors challenging climate change measures is not theoretical. For example, TransCanada brought a US$15 billion claim against the United States under the North American Free Trade Agreement (NAFTA) after the Keystone XL pipeline was originally denied approval.[3] In 2019, Westmoreland Coal sued Canada for $470 million, also under NAFTA, as a result of the state of Alberta's policy to phase out coal-power by 2030.[4]

The threat or risk of such claims against Australia, even if unlikely to succeed or lead to large damages, nevertheless gives foreign investors unwarranted and excessive leverage to influence climate change policy in Australia.[5] One way to address this risk is simply to terminate the existing BITs. As discussed in section 4 below, the evidence is inconclusive as to whether BITs in fact positively impact foreign direct investment flows. Alternatively, Australia's existing BITs could be renegotiated to include appropriate safeguards against such claims.

## 3. Clauses that should be included in a renegotiated agreement

As noted in the Discussion Paper, FTAs negotiated by Australia in recent years contain clauses aimed at safeguarding the Australian government's right to regulate. The investment chapter

[2] *Paris Agreement*, opened for signature 22 April 2016 (entered into force 4 November 2016).
[3] *TransCanada Corporation and TransCanada PipeLines Limited v The United States of America*, ICSID Case No ARB/16/21 (later discontinued after the project was subsequently approved).
[4] *Westmoreland Coal Company v Government of Canada*, ICSID Case No UNCT/20/3. This dispute is still pending.
[5] For a discussion of the types of regulatory chill and the evidence for them in the climate change context, see Kyla Tienhaara, 'Regulatory Chill in a Warming World: The Threat to Climate Policy Posed by Investor-State Dispute Settlement' in (2018) 7(2) *Transnational Environmental Law* 229.

of the Peru-Australia Free Trade Agreement (PAFTA),[6] for example, contains the following clauses:

> Article 8.16: Investment and Environmental, Health and other Regulatory Objectives
>
> Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental, health or other regulatory objectives.
>
> Article 8.18: General Exceptions
>
> Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between investments or between investors, or a disguised restriction on international trade or investment, nothing in this Chapter shall be construed to prevent the adoption or enforcement by a Party of measures:
>
> (a) necessary to protect human, animal or plant life or health;
>
> (b) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Chapter;
>
> (c) imposed for the protection of national treasures of artistic, historic or archaeological value; or
>
> (d) relating to the conservation of living or non-living exhaustible natural resources.
>
> The Parties understand that the measures referred to in subparagraph 1(a) include environmental measures to protect human, animal or plant life or health, and that the measures referred to in subparagraph 1(d) include environmental measures relating to the conservation of living or non-living exhaustible natural resources.

Any future renegotiated agreements entered into by Australia should include such clauses. Any general exceptions clause should explicitly clarify that the measures it refers to include measures relating to climate change. An alternative approach is to include specific exceptions to particular protection standards, for example by clarifying that regulatory measures, including those relating to climate change, will not amount to indirect expropriation or unfair treatment provided that they are not applied in a discriminatory manner.

Such clauses will not, however, remove entirely the risk of claims challenging climate measures, even if such claims would be unlikely to be successful. After all, investment tribunals never negated the theoretical possibility of host-states taking measures to protect certain public goods and interests, but rather have placed strict, ad hoc and often unpredictable

[6] *Free Trade Agreement between Australia and the Republic of Peru,* signed 12 February 2018 [2000] ATS 6 (entered into force on 11 February 2020) Ch 8.

limitations on their ability to do so.[7] Investors could still bring speculative claims that Australia would have to defend. The Discussion Paper notes that Australia's modern FTA practice has involved excluding investor-state dispute settlement (ISDS) claims against public health measures. Article 29.5 of the Trans-Pacific Partnership (TPP), as incorporated by the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, gives states the power to prevent investors from bringing claims challenging a tobacco control measure under the TPP's investment chapter.[8] Article 14.21(1)(b) of the Indonesia-Australia Comprehensive Economic Partnership Agreement also excludes ISDS claims 'in relation to a measure that is designed and implemented to protect or promote public health'.[9] This submission therefore also proposes that renegotiated BITs similarly carve out claims challenging climate change measures from ISDS.

Alternatively, renegotiated BITs could exclude ISDS entirely. Although this would be a departure from previous practice, as discussed in the next section, there are significant arguments that support this approach. First, the evidence that there is positive correlation between investment inflow and ISDS is at best inconclusive. Secondly, ISDS accords — by definition — a stronger negotiating position to foreign investors as opposed to the legal and political position of domestic investors, Indigenous peoples, the scientific community, etc.

## 4. The impact of BITs

### 4.1 On the flow of foreign direct investment

Terminating BITs or renegotiating them to limit or exclude ISDS is not necessarily going to have any impact on flows of foreign direct investment into Australia since it is not clear that there is any causal relationship between BITs or more specifically ISDS and increased foreign direct investment. Australia is considered a low-risk country in which to invest,[10] and there are other options for investors to protect against themselves, such as domestic courts, investment guarantees and political risk insurance. This submission only considers the relationship between BITs and foreign direct investment generally, rather than commenting on Australia's specific existing BITs.

A 2017 review of 35 quantitative studies of the impact of BITs on foreign direct investment flows found mixed results.[11] While a majority of studies found that BITs had a positive impact on foreign direct investment flows in at least some circumstances and to some extent, a 'sizeable minority' found no effect. Furthermore, the quality of studies varied. Jonathan

[7] For example, Kate Miles has noted that in the *Clayton v Bilcon* award the NAFTA tribunal placed undue emphasis on the expression 'community values' as grounds for recalling the permit of an investment ignoring the fact that the decision squarely fell within Canadian environmental law: Kate Miles, 'Investor-State Dispute Settlement: Conflict, Convergence, and Future Directions' (2016) *European Yearbook of International Economic Law* 273.

[8] [2018] ATS 23(entered into force 30 December 2018).

[9] [2020] ATS 9 (entered into force 5 July 2020).

[10] Australia ranked 14th in the World Bank's ease of doing business rankings for 2020. The World Bank, *Doing Business 2020: Comparing Business Regulation in 190 Economies* (Report, World Bank Group 2020).

[11] Jonathan Bonnitcha, Lauge N Skovagaard Poulsen and Michael Waibel, *The Political Economy of the Investment Treaty Regime* (Oxford University Press 2017) 158–64.

Bonnitcha and Emma Aisbett have argued that those studies that better accounted for the fact that two countries may have negotiated a BIT because of an increase in foreign direct investment flows between them and the fact that countries may enter into a BIT at the same time as adopting other measures to encourage foreign direct investment tended to find no causal link between BITs and an increase in foreign direct investment.[12] Furthermore, the 2017 review also noted three recent studies that have found that BITs providing for ISDS do not lead to an increase in foreign direct investment flows any more than those which do not contain such provisions.[13]

### 4.2 On the position of foreign investors in political deliberation and legal reform

We note the fact that in its 2016 report on its inquiry into the TPP agreement, the Joint Standing Committee on Treaties observed that 'the evidence for regulatory chill is anecdotal'.[14] However, it is a matter of fact that, regardless of its systemic effects, ISDS gives foreign investors a privileged legal and political position that other economic and political actors lack. We contend that in a liberal democracy this is a problem in its own right and regardless of its tangible effects (which can be, of course, further aggravating factors). The promotion and protection of foreign direct investment has often been justified as a factor that leads to development. However, as Anil Yilmaz-Vastardis has noted, ISDS means that foreign investors have no reason to care about the existence of a functional judicial system in the host-state. If anything, they could benefit from dysfunction and corruption if it is directed against their wage-seeking employees, or those who oppose their investment, while at the same time avoid the negative effects of such dysfunctions when it comes to protecting their own interests.[15] Given Australia's role as a major developmental partner in the Asia-Pacific it is doubtful whether the continuing adopting of such an anti-developmental measure is morally justifiable or (geo)politically smart.

Relatedly, we contend that regardless of its outcomes, ISDS gives foreign investors a seat at the table of political deliberation that no other actor occupies. Through ISDS, one type of participant in the political and legal process has the privilege of bypassing entirely this process as well as domestic courts in order to enforce their preferences. If we examine the history of

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[12] Jonathan Bonnitcha and Emma Aisbett, 'Submission to the Productivity Commission's Review of Bilateral and Regional Trade Agreements', available online at: https://www.pc.gov.au/inquiries/completed/trade-agreements/submissions/sub045.pdf. See also E Aisbett, 'Bilateral Investment Treaties and Foreign Direct Investment: Correlation versus Causation' in Karl Sauvant and Lisa E Sachs (eds), *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties and Investment Flows* (Oxford University Press 2009).

[13] These were Alex Berger, Matthias Busse, Peter Nunnenkamp and Martin Roy, 'More Stringent BITs, Less Ambiguous effects on FDI? Not a BIT!' (2011) 112 *Economics Letters* 270; Axel Berger, Matthias Busse, Peter Nunnenkamp and Martin Roy, 'Do Trade and Investment Agreements Lead to More FDI? Accounting for Key Provisions inside the Black Box' (2013) 10 *International Economics and Economic Policy* 247; Clint Peinhardt and Todd Allee, 'Devil in the Details? The Investment Effects of Dispute Settlement Variation in BITs' in Karl Sauvant (ed), *Yearbook on International Investment Law & Policy* (Oxford University Press 2010–2011).

[14] Joint Standing Committee on Treaties, *Trans-Pacific Partnership Agreement* (Report No 165, November 2016) para 6.59.

[15] Anil Yilmaz-Vastardis, 'Justice Bubbles for the Privileged: A Critique of the Investor-State Dispute Settlement Proposals for the EU's Investment Agreements' (2018) 6(2) *London Review of International Law* 279.

international investment law, we easily realise that this is a feature and not a bug of ISDS as a whole, which was designed in order to give foreign investors legal and political privileges that go beyond national legislation and, importantly, national political processes.[16] Given the explosive nature of economic inequality in the early twenty-first century such provisions are likely to both further exacerbate material inequality and to further undermine trust in the political and legal system opening up space for populist-nativist forces that seek to undo international economic integration as a whole. At the very least, political debate should not take ISDS for granted and demand that opponents make a case against such provisions. Rather, the burden of proof falls squarely on the shoulders of the defenders of the institution, especially given its lax relationship to investment inflows and the tensions between a two-tier justice system and the basic tenets of liberal democracy.

## RECOMMENDATIONS

**In light of the above we put forward three recommendations:**

1) **Australia should terminate its existing BITs.**
2) **Alternatively, Australia should renegotiate its existing BITs so as to exclude ISDS either entirely or in respect of claims challenging climate change measures.**
3) **If Australia decides to maintain ISDS clauses in renegotiated BITs, it should introduce clauses that explicitly guarantee the right to regulate both in general and in regards to particular areas, including public health and, notably, climate change.**

[16] Martti Koskenniemi, 'It's Not the Cases, It's the System' (2017) 18 *Journal of World Investment and Trade* 343; Ntina Tzouvala, 'The Ordo-Liberal Origins of Modern International Investment Law: Constructing Competition on a Global Scale' in John Haskell and Akbar Rasulov (eds), *New Voices and New Perspectives in International Economic Law* (European Yearbook of International Economic Law, Springer 2020); Ntina Tzouvala, 'The Academic Debate about Mega-Regionals and International Lawyers: Legalism as Critique?' (2018) 6(2) *London Review of International Law* 189.