



# HOUSE OF LORDS

Unrevised transcript of evidence taken before

## **The Select Committee on the European Union**

External Affairs (Sub-Committee C)

Inquiry on

## **TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP**

*Evidence Session No. 19*

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*Questions 208 - 223*

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9.30 am

Witnesses: Dr Lauge Poulsen and Rt Hon Lord Goldsmith QC

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Members present

Lord Tugendhat (Chairman)  
Baroness Bonham-Carter of Yarnbury  
Baroness Coussins  
Lord Foulkes of Cumnock  
Baroness Henig  
Lord Jopling  
Lord Lamont of Lerwick  
Lord Maclennan of Rogart  
Baroness Quin  
Lord Radice  
Earl of Sandwich  
Lord Trimble  
Baroness Young of Hornsey

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**Examination of Witnesses**

**Dr Lauge Poulsen**, Research Fellow, Nuffield College, University of Oxford, and Senior Research Fellow at University of London, SOAS, and **Rt Hon Lord Goldsmith QC**

**Q208 The Chairman:** Lord Goldsmith and Dr Poulsen, thank you for coming before us, and thank you for coming at an earlier time than originally envisaged. As you both know, this is part of our inquiry into TTIP, the Transatlantic Trade and Investment Partnership. We have been conducting this inquiry for quite some time now, and we are getting quite near the end. An issue that has arisen, not so much in the evidence that we have received but in written representations that have been made to us, concerns the investor-state dispute settlement provisions. We have received quite a number of representations on that. The Commission is now conducting an inquiry, but it seemed to us that there is a sufficient degree of public concern that we ought to try to form a view. We are very grateful to you for agreeing to come before us. We will each ask a number of questions and there will be supplementaries. You are both welcome to answer the questions, but if one of you answers and the other agrees, there is no need to go over the same ground.

Can I ask a very straightforward question at the beginning directed to Lord Goldsmith? With all your experience of the matter, can you set out the background to the inclusion of ISDS mechanisms in bilateral investment treaties between EU member states and third countries since the Lisbon treaty entered into force? At whose instigation are they typically included?

**Lord Goldsmith:** With pleasure, Lord Chairman. I shall say one word by way of background. It is important to understand that the investor-state dispute settlement procedures—the ISDS—are simply a mechanism for giving effect to substantive protections which are agreed. The concept is that investment treaties, which are typically bilateral though some are multilateral, set out between those states that join them the protections which each will agree to accord to the investors from the other state. The ISDS is not in itself a substantive measure of protection; it is a mechanism for providing a dispute resolution mechanism where there are questions about whether those protections are being provided. Once upon a time, investors were protected by their national state through diplomatic protection or, in even earlier times, through military protection. Gunboats were how investors were protected. Then it moved into diplomatic protection, which has a lot of issues connected with it, such as the politicisation of what are in fact investment disputes. Bilateral investment treaties are a more recent development. We think the first BIT was concluded in the late 1950s in which an EU country—Germany—was very much involved. There is now a very substantial number of bilateral investment treaties. Lisbon gave jurisdiction to the EU to conclude those agreements and started the process of the EU taking over bilateral investment treaties, leaving in place regulation which grandfathered those which are already in place and concluding new agreements to provide for them. That is the background to how they came into existence. The Committee may well come on to this, but they are very heavily used by investors from many states including from EU states. I am happy to elaborate on that, if and when you want it.

**The Chairman:** At whose instigation are they generally?

**Lord Goldsmith:** Generally, it is the capital-exporting countries that instigate them because it is their national companies and individuals from their countries who generally are investing in the capital-importing countries, and therefore they are the ones who want to see the protections in place, but they are reciprocal so they work both ways. Although the majority of investment arbitration claims are still brought by investors from capital-exporting countries, increasing numbers are brought by nationals from developing countries, so that gap is narrowing.

**The Chairman:** Dr Poulsen?

**Dr Lauge Poulsen:** I have nothing else to add.

**Q209 Lord Lamont of Lerwick:** Building on what you said, can you tell us what has been the experience of EU member states as regards these mechanisms? In particular, what sorts of claims have been brought against them and what sort of outcomes have resulted? How have EU investors taken advantage of them? Have they put the agreements to wide use against third countries?

**Dr Lauge Poulsen:** In terms of claims against European states, the vast majority of investor-state arbitrations have been claimed against new EU members state, eastern European countries, where a vast range of government measures have been targeted by investor-state arbitration. For instance, in Poland, there was a range of claims in the 1990s around Poland's environmental regulation. In the Slovak Republic, there have been claims regarding the roll-back of the liberalisation of the national health insurance market. In Hungary and Romania, there have been claims concerning the roll-back of state aid in the electricity sector. Western European EU members have also been subject to claims. For instance, Germany has been subject to two quite notable claims, both by Vattenfall, the Swedish energy company, and Belgium has been subject to a very large claim by a Chinese investor. Greece

has been subject to claims for the measures it took during its financial crisis. Spain has been subject to claims. There has been a wide range of measures that have targeted not just eastern European members but increasingly western European countries, including Germany.

**Lord Lamont of Lerwick:** Why western European countries as well? When you say “increasingly”, one can understand why there would be eastern European countries, but why is it suddenly becoming more west European countries and on what sort of issues?

**Dr Lauge Poulsen:** To go back to what Lord Goldsmith mentioned before, these are reciprocal agreements, so when you have an increasing inflow of capital from developing countries, suddenly developing-country investors can also use these agreements to file claims against western European Governments. In the case of Germany, the claims were under not a bilateral investment treaty but under the Energy Charter Treaty, which was entered into by European countries and Russia in the early 1990s.

**Lord Lamont of Lerwick:** Are these disputes always about public policy, or could they be against a private entity as well?

**Dr Lauge Poulsen:** No, these would typically be disputes about government regulation. They could deal with decisions of courts or legislation. They are not commercial arbitration proceedings between private companies or between a private investor and a Government acting in a commercial capacity.

**Lord Goldsmith:** Dr Poulsen has talked about claims against EU states. I think it is important to put this in context. EU member states are among the most prolific users of investment protection in looking after the interests of their nationals. If you look at the number of cases started between 2008 and 2013—all investor-state cases across the world—more than half of them were initiated by EU investors. Classic claims are about expropriation, nationalisation, the removal of licences without compensation and that sort of thing. It is true that some claims have been brought against EU states. They tend to be eastern

European. It is worth the Committee remembering that claims can be brought, but that does not mean that they will succeed. Claims have to be for a breach of one of the specific protections which the treaty provides for, whether it is bilateral or, as Dr Poulsen says, multilateral, like the Energy Charter Treaty. They would be for expropriation, except for a proper public purpose and with proper compensation or reasonable compensation—the words differ—for fair and equitable treatment, non-discrimination and those sorts of area. Ultimately, it is a claim against the treatment by the state, but it would not necessarily be about public policy; it could be a claim that an investor has been treated unfairly, even as a result of the way that the courts have operated. There are claims against the United States, for example, under the North American Free Trade Agreement arrangements, which include claims against the United States for that reason.

**Q210 Baroness Quin:** That is very helpful, but I am just thinking about the number of cases that there have been. In the Polish case, which I think you said was about a challenge when the Government wanted to roll-back some liberalisation in the health sector, which seems quite pertinent to some of the concerns that have been raised here, did the outcome involve a subsequent change in government policy or was it simply to do with some aspect of compensation to a particular investor?

**Dr Lauge Poulsen:** It was a case against the Slovak Republic, not Poland. The investor won about £18 million, which was paid out by the Slovak Republic. Later, the constitutional court in the Slovak Republic also decided that the measures were unconstitutional, but another claim has been brought by the same investor trying to pre-empt additional reforms in the Slovak national health sector for insurance. It is still pending, and we do not know what the outcome will be.

**Lord Goldsmith:** I understand that this is a case which causes concern. It is the Achmea case. It is worth bearing in mind that the actual challenge was on the ban on the

expropriation of profits, as opposed to the concept of nationalisation or renationalisation and, as Dr Poulsen said, it turned out that by Slovak national law what had taken place was unlawful. The constitutional court declared it unlawful.

**Q211 Baroness Coussins:** You said that not all claims succeed, but can you say what the success rate has been so far in terms of claims against EU member states and whether there is any differentiation between the success in claims against eastern and western European countries?

**Dr Lauge Poulsen:** On the exact statistics for western European member states, I am not quite sure. One has to remember that we are not entirely clear how many claims are made against EU member states and others because some claims can be pursued under arbitration rules that do not necessarily require that the fact that there is a claim should come to public knowledge. In general, about 30% of claims have been resolved in favour of investors, a little less than 30% have been settled—the content of those settlements is typically unknown, but many can be assumed to be in favour of investors, and the remaining approximately 40% have been decided in favour of the state. Without knowing exactly, I think that the statistics for European countries could be about the same. That is the general picture.

**Q212 Earl of Sandwich:** We have heard in evidence that the UK for some reason does not get into so many disputes and that there are not so many settlements. Can you explain why that might be?

**Dr Lauge Poulsen:** Sure. The main reason is that the United Kingdom has traditionally not entered into investment treaties with major capital-exporting states, so when we think of the potential scenario that could result from the EU-US agreement, the more relevant set of experiences for the United Kingdom to consider is that of Canada. Canada entered into an investment treaty with the United States in the 1990s, which was Chapter II of the North American Free Trade Agreement. Following that agreement, the last time I checked Canada

has been subject to 34 or 35 claims. About a handful of these claims have been lost and a couple of other claims have been settled. A couple of these settlements have been in favour of the investor, and I do not think there is any reason to expect the UK not to be subject to a similar number of claims, for the very reason that 8% of US outward foreign direct investment stock is in Canada while 13% is in the United Kingdom. Bearing that statistic in mind we would expect more claims against the United Kingdom, all else being equal. All the top 100 of the top 500 companies in the United States operate in the United Kingdom in all sectors of the UK economy, ranging from services, manufacturing and finance to natural resources. It is difficult to claim that the UK should somehow be exempt from claims by US investors when Canada was not.

**Lord Goldsmith:** I disagree with that very strongly. I think that is an odd way of looking at it. I think the reason why the UK is not subject to successful claims is the nature of the protections that exist already under UK law and practice. Claims can be brought only where there is, usually, an arbitrary or capricious action of the state in relation to an investment, and there is a range of reasons why that does not happen here. We have a strong democracy, and we have strong scrutiny by Parliament of measures such as expropriation. We have the Human Rights Act and the European convention, which provide strong protection against those sorts of events. We also have a very objective, fair justice system that deals with claims where people have issues. So I would not expect there to be significant claims. Claims may be brought against the UK—people do that from time to time, as I said—but successful claims would be very limited.

**Q213 Lord Trimble:** Lord Chairman, I think my question 3 follows on very naturally from what Lord Goldsmith has said. It refers to written evidence from the TUC about the ISDS, but the substance of the view is that we have a robust legal system in the United Kingdom—in which case do we actually need to have these dispute settlement systems?



**Lord Goldsmith:** The point is that it is a reciprocal arrangement. We cannot say, “You do not need protection against what we do, but we want protection against what you do”. I think you have to recognise the reciprocity, and therefore you have to accept that in order to get protection for our nationals in other countries.

**Lord Trimble:** I accept that, but in your opening comments you said that the ISDS is merely a process for handling claims and that the really important thing is the substantive protections in the treaties. You mentioned a couple of things such as protection against expropriation and unfair treatment. Is that the sum total, because it seems to me that the really important thing is, as you say, the substantive protection in the treaties, and the ISDS is just a matter of enforcing that? I therefore wonder what the full extent is of the protection that is in the treaties.

**Lord Goldsmith:** That is a matter for agreement. There are some principles of customary international law that are likely to be included, but they are to do with no expropriation except against compensation. Typically you would include expropriation, direct or indirect. Fair and equitable treatment is commonly included, but you can define what you mean by fair and equitable treatment. What we have seen of the Canadian-EU proposed free trade agreement defines that quite closely, and one of the things that it will do, therefore, is not touch so much perhaps on the regulatory space. You can provide for a most favoured nation clause—that is quite common. No discrimination will be quite common as well. Those are the sorts of areas that will typically be included in an investment treaty, but it is a matter for negotiation and agreement.

**Lord Trimble:** And presumably the TTIP negotiations have not reached the point of discussing these things yet.

**Lord Goldsmith:** Yes, that is right.

**Q214 The Chairman:** Dr Poulsen, I think that you were going to add something, but I did not turn to you.

**Dr Lauge Poulsen:** I have a couple of comments. First of all, I am not quite clear why we should not expect similar experiences in the UK that Canada has experienced. Canada is also a strong democracy. Canada also has strong protections for foreign investors. I have seen no evidence to the contrary. Canada also has independent courts that are effective in adjudicating disputes, so I am not quite clear where the systematic differences between Canada and the UK are so that we are in the position to say that the UK will be insulated from claims. Canada is no banana republic.

When it comes to why we should include these sets of provisions in a US agreement, again I am not quite clear what the actual problem is in protecting foreign investment in the United States. The United States has a strong tradition, just like the UK, of protecting capital. It has independent and efficient courts. So it is not entirely clear what exactly the political, economic or institutional rationale is for providing an additional set of protections to what is already there in the United States.

**Lord Trimble:** Look at the way BP was treated by the American Government and courts. That was pretty indefensible.

**Dr Lauge Poulsen:** First of all, in any court system we can come up with instances where an individual investor or person has been disgruntled about how they have been treated by a court system. What we need in order to justify an internationalised dispute settlement mechanism that allows investors to sidetrack domestic courts is systematic concrete evidence that courts in the United States, or even courts in Europe, are somehow systematically biased against foreign investors. I have not seen that evidence thus far.

**Lord Goldsmith:** I just see that as a misunderstanding entirely of the need for protection. First of all, the UK is a party to, I think, 90 bilateral investment treaties. As far as I know,

there have been only two claims against the UK, one of which was withdrawn, the other was complicated and to do with the Channel Tunnel. I think there is experience already as to how this operates as far as the UK is concerned. With the US, there are issues. The Committee may know about the Loewen case. In the Loewen case a Canadian investor was sued in the courts of Mississippi on a commercial dispute for about \$7.5 million—that was all it was. The Mississippi court, with a judgment by jury, came up with a judgment of hundreds of millions of dollars. The Canadian investor was, he believed, very badly mistreated in the Mississippi court and accused of all sorts of things by counsel. In order to appeal, he had to put up a bond that was a multiple of the judgment, which was virtually impossible. He ended up spending \$125 million in a settlement, because that was all that could be done. That would not happen in a London commercial court. I do not think it would happen in New York either, but it can happen in parts of the United States, unfortunately, as reasonable protection.

**The Chairman:** We need to get on to some other questions, but Dr Poulsen, you wanted to comment.

**Dr Lauge Poulsen:** A brief rebuttal. First of all, after that claim there was tort reform in Mississippi to try to address that problem. Secondly, investor-state arbitration did not help the investor in that case, so I do not think it is a useful anecdote to bring in to justify investor-state arbitration, because investor-state arbitration on NAFTA did not help.

**Lord Goldsmith:** I will send the Committee a note as to why that is not actually a relevant comment.

**Q215 The Chairman:** Can I just ask one supplementary question before we go on to the next question? Who generally bears the costs of litigation?

**Lord Goldsmith:** It is normally both parties, although there is an increasing tendency for the unsuccessful party to bear some of the costs of the arbitration. That is not specifically

provided for in the ICSID system. It can easily be provided for in a treaty if one wants to, but generally the losing party should pay, or generally both parties should bear their own costs. On the whole, investors are not ordered to pay, but states quite frequently are.

**The Chairman:** But if the state wins, presumably it does not pay.

**Lord Goldsmith:** No, it would not pay if it wins, unless it has been thought to be guilty of some unreasonable conduct in the conduct of proceedings.

**Q216 Lord Foulkes of Cumnock:** Lord Chairman, this is much more interesting because the two witnesses disagree with each other. They are by far the best we have had so far. Lord Sandwich has also anticipated the first part of my question, but that helps because Dr Poulsen said we can expect more claims against the United Kingdom. It has been suggested to us that if there are claims to—to use your phrase—“protect private capital”, that could create problems. Let us take a scenario in the United Kingdom in which there had been lots of American investment in the NHS and we wanted to pull back. Would that cause tremendous problems for a Government wanting to reverse policies on the NHS?

**Dr Lauge Poulsen:** I think that that potential scenario would depend in part on the sorts of promises that are made to American investors in the sector and whether the measures taken would undermine the business of those American investors operating here. Again, a potentially relevant case is the case against the Slovak Republic trying to roll back the liberalisation of the national health industry. The Slovak Republic lost about £18 million which, related to the size of the UK economy would be about £0.5 billion against the UK. As economists would say, £0.5 billion here, £0.5 billion there, adds up to real money in the end. As to whether we can expect there to be significant problems for the NHS, I do not think that we should exaggerate that risk, but it is difficult to sit here and argue that it can be ruled out.

**Lord Foulkes of Cumnock:** Lord Goldsmith was shaking his head. He might be advising the next Government.

**Lord Goldsmith:** I am quite happy to do that, if asked. The Slovak case was ultimately decided not on the question of the change in policy but on the question of the prohibition on the repatriation of profits, which is quite a common problem in international trade. The Canada-EU agreement proposes a number of specific protections which are carefully drawn up so that you maintain the regulatory space and protect public health and things of that sort. That is why it is very important that the substance of what is agreed is more important than the mechanism for dealing with it.

It is also important to note that it has never been impossible for states to nationalise. It is common that it happens. It is the classic example. It is nationalisation on a discriminatory basis or nationalisation without compensation which causes the problem in investment protection. I do not know whether this is the reason that we disagree, but the firm in which I am now a partner does a great deal of investment protection work across the world and therefore we have seen many examples of how states can act in a way which creates legitimate claims and cases where people would like to make claims but are unable to because the protections do not cover the particular conduct and the Government were justified in doing what they were doing.

**Q217 Baroness Henig:** Can I change the focus to United Kingdom investors? To what extent have they taken advantage of these mechanisms in existing UK and EU investment treaties and how would you weigh up the costs and benefits to them of the inclusion of this mechanism in TTIP?

**Dr Lauge Poulsen:** We are aware of around 30 claims that have been filed by UK investors. The first bilateral investment treaty claim was under a UK investment treaty with Sri Lanka. In a couple of these cases, UK investors have been successful, for instance, against Argentina

for measures it took after its financial crisis. But I would like to add—and Lord Goldsmith and I are going to disagree again—that the fact that UK investors have used these agreements and have occasionally been successful in obtaining compensation is not necessarily evidence that these agreements are necessary for UK investors to protect against political risks, such as expropriation. If a UK investor is genuinely concerned about expropriation in a country like India, it can take out political risk insurance against those acts, from either the UK Government, MIGA, which is an insurance provider under the World Bank, or the large private market that insures against political risks, such as expropriation. The sorts of risks that are included in insurance do not cover the totality of the risks that are covered by investment treaties but get quite close.

Secondly, if you are genuinely concerned as an individual UK investor about the operation of the courts in the host state, you have the ability to negotiate an investor-state contract with that Government that provides for recourse to investor-state arbitration. I am not saying that investment treaties are not important for the protection of foreign investment, but that they are not necessary for the protection of foreign investment because there is already a series of layers of protections that are available to UK investors and others.

**Lord Goldsmith:** UK investors have used this in a number of areas. I think that there are two fundamental things that investment protection is providing. One is a guaranteed level of protection. Even if a national law provides for protection, it is open to the nation state to remove that protection. I have examples of where countries have removed protections that they had promised and had put into agreements but were just removed because it is all subject to national law. First of all, the protection provides a level of protection under international law, and secondly, it generally provides an opportunity for having your dispute determined by an objective independent tribunal, rather than by a national court. Sometimes national courts act against an investor because they are not prepared to act against their

own Government, and sometimes it is simply because the Government pass laws which the national courts have no option but to obey.

Insurance may be available—it is a very interesting observation—but the other suggestion is that investors can negotiate investment agreements. They can from time to time, but unless they also provide for the application of international law and for an international dispute resolution mechanism, they do not achieve anything. That is only saying that you have a private investment treaty rather than a public investment treaty. I do not really see the benefit of that. That is why the protections are there.

**Baroness Henig:** I am trying to get a handle on what is causing the differences between you. Would it be fair to say—it may not be—that Dr Poulsen is telling us what should happen and Lord Goldsmith is telling us what actually happens? Is that where the difference is coming from?

**Dr Lauge Poulsen:** I would strongly disagree with that statement. There has been comment to the effect that the reason I take this position is because I sit in the ivory tower, whereas Lord Goldsmith is out in the real world. I am not quite sure that that is true. The important point is that the Committee is supposed to be discussing the necessity for these sets of protections, not in general but in an agreement with the United States. It is up to the proponents of investor-state arbitration to provide us with strong political and economic justifications for why these sets of provisions are necessary in the United States.

Secondly, even if you disagree with all the criticisms that are occasionally made against investor-state arbitration, the fact of the matter is that there is strong and growing discontent with the prospect of allowing all American investors to sue all EU Governments outside European courts. While you may disagree with that perception, that discontent—which, incidentally, we saw in the House of Commons just two days ago—is important because the agreement has to be ratified. Ultimately you need very strong justifications for

why we would want to risk the political agreement for the transatlantic trade agreement as a whole derailing because provisions are included that, in the case of the United States, are not even necessary.

**Lord Goldsmith:** I have not set out to disagree with Dr Poulsen at all. I have set out to try to assist the Committee in an important task. To my mind, the fundamental point is that no one has yet come up with a better system for investment protection than a system of protections that are negotiated between the member states or groupings of member states with an independent, objective system, such as international arbitration, to enforce them. I am sure that the Committee would do a great service if it were to make observations on the extent of protections and on whether it finds, for example, that there are aspects of the Canada-EU free trade agreement which would be valuable to bear in mind when negotiations take place. I do not think it is for the proponents. Investment protection is there because it serves a very real purpose because it is better than diplomatic protection. Diplomatic protection, even when it moved away from military protection, still politicised these disputes in an unsatisfactory way. There may be arguments about elements that could be negotiated or should be changed, but I do not see that there is a better system than this sort of agreement.

**Q218 Baroness Young of Hornsey:** Before I ask the question that I have down before me, I have a question that kind of follows on from what Lord Goldsmith said. In the written evidence we have received from the TUC, it notes that Australia has recently reaffirmed its refusal to include any such provisions in any future trade agreements. Would you like to comment on that, especially in the context of what you have just said about the necessity of having ISDS?

**Lord Goldsmith:** I thought that it was the other way round. I must check. I thought what happened was that Julia Gillard's Government announced that they were no longer going to



include ISDS in their trade agreements, but that was then reversed under the new Government, but I had better check that in the light of what you say.

**Baroness Young of Hornsey:** Even if that was the case, it would still be interesting to know what your view is on why that decision had been arrived at.

**Lord Goldsmith:** There are a number of theories about why Julia Gillard's Government reached that view. One of them may have been the very controversial case brought by Philip Morris, which challenged the Australian plain-packaging requirement. We do not know whether that case is going to succeed because that arbitration is still continuing. If that is an area of concern, one can cover that by the protections and carve-out, as the EU-Canada trade agreement seeks to do. For example, it carves out protections for the benefit of public health. One can do that. Whether that was the reason for it, or whether it was some other reason, I do not know.

**Dr Lauge Poulsen:** I think that one of the reasons was that, according to the Australian Government of the day, there was a perception that you should have very strong justifications for giving all foreigners the right to sidetrack domestic courts. When we talk about investment treaties, in the 2005 investment treaty between Australia and the United States, the Australian Government argued that there is no need for an additional adjudication mechanism at the international plane when we talk about Australian or US courts. That was the justification for excluding those provisions in the US-Australia free trade agreement, and the United States hesitantly agreed to exclude them, which it is important to keep in mind. It is the same justification that the European Parliament is using when saying that the EU can include these sorts of provisions in free trade agreements but only when necessary and justified. I would challenge proponents of investor-state arbitration to tell me why it is necessary when we talk about the United States of America, given its court system and its existing levels of protection.

**Q219 Baroness Young of Hornsey:** Thank you. If I may I will now go on to my other questions. Lord Goldsmith, where do you think there are legitimate causes for concern in the mechanism, and which concerns are less well founded? Perhaps you have already elaborated on some of those. Is there a way of reconciling public concerns with an ISDS mechanism?

**Lord Goldsmith:** If I may say so I think that is absolutely the point. A number of criticisms are made of investor state dispute resolution and ISDS that are ill founded, such as that this is a secretive process or is not objective. One looks at the way tribunals are constituted. There is greater transparency in any event in, for example, ICSID—the International Centre for Settlement of Investment Disputes—which is the principal system through which these disputes get resolved. Generally the decisions are in fact produced. It is true that in certain other systems they are not. There is about to be a new regulation on transparency—the UNCITRAL system, which is the other very popular system for investor state arbitration. That comes into force this year. So I do not think that those are justified concerns.

The area where there is legitimate scope for discussion as to the extent of the protections relates to how the regulatory space of a particular country may be affected, but that is something you reconcile—if I may use your term, Baroness Young—by the substantive protections that are provided. I come back to the Canadian-EU example, where people obviously thought very hard about how you carve out the areas that matter. You cannot just say, as some people do, that the state should be allowed to do what it wants. I have examples of cases that I have been arguing against states that have simply taken assets without compensation. Belize has taken a telephone company but has still not paid compensation years after taking it. It was entitled to nationalise the telecommunications if that is what it wanted to do, but not without any compensation. That dispute still rolls on. It is important to have the substantive protections, but you reconcile those areas. The

principal area, to my mind, is interference in proper regulatory activity by the state by the substantive protections that we put in place.

**Dr Lauge Poulsen:** Very briefly, first, I doubt the case referred to by Lord Goldsmith—the US refusing to pay compensation for expropriation. Secondly, there is a range of criticisms against investor state arbitration. I do not think we have time to go through all of them here, but the most important question that one has to ask oneself is: why can you not find a single serious economist who can tell you that it is useful to give one class of investors—that is, foreign investors—rights that domestic investors do not have, the most important right being recourse to investor state arbitration? That is institutionalised inequality, and it would be very hard for you to invite any economist to come here and tell you that that is somehow a useful idea. That is the most important thing to consider when you think about the criticisms of this regime. The key thing that we are talking about today is an agreement with the United States. Why is this necessary? I do not think we have heard answers to that question.

**Baroness Quin:** I do not know whether Lord Goldsmith wants to respond to that.

**Lord Goldsmith:** I would much rather hear your question, Baroness Quin.

**Q220 Baroness Quin:** My question follows on from Baroness Young's question. In two lots of written evidence to us, the phrase has come up that ISDS creates "a regulatory chill" that stays the hand of government to regulate in the public interest for fear of litigation. I just wondered whether you are aware of concrete examples of this.

**Lord Goldsmith:** It is suggested that there may have been that effect as a result of the Philip Morris case against Australia in relation to a couple of countries that were thinking of introducing plain packaging for cigarettes. I am not sure that there is empirical evidence yet that that is the case, but that is the sort of area that one would look at. The case has not been decided, so I cannot judge what it will be, but it is a pretty extreme case of an

investment claim. It has created a lot of controversy within the community that deals with these cases all the time as to whether it is a legitimate claim or not. It was not an expected claim. That is why I think it would be legitimate when one is negotiating an arrangement with the United States to look at whether there are carve-outs or definitions of what fair and legitimate expectation may be.

Let us take Dr Poulsen's point about courts. Anyone who does any business close to the United States knows that there are issues in relation to state courts and to jury awards, some of which are corrected and some of which are not. I gave the Mississippi example. Maybe that has now been corrected by legislation. Still, it was a very difficult issue for the investor involved. If you define carefully the level of absence of protection by the courts you are concerned with, you can give legitimate protection. I do not know whether Dr Poulsen is right that no economists have come before this Committee to explain the benefits, but I have always understood that the principal benefit of investment protection is that it encourages foreign investors to invest. They do not have to invest in these countries. If they do not think their investment is protected or if they think it will be taken away, that is the argument for why they need protection. Maybe one could do something else, but that, I think, is the reason for it.

**Q221 Lord Jopling:** You have both referred at various times to the Canadian agreement. Let us turn to that agreement and discuss it in terms of its relevance to the TTIP negotiation. I think it would be helpful if you could draw your various points together and tell us the extent to which you think CETA highlights various problems that have been expressed over particular innovations and the key features of it, with what you know of the Canadian agreement. How much of it is relevant and helpful, and what other arrangements would you like to see in the TTIP negotiation that would improve the Canadian deal?

**Lord Goldsmith:** If I may, I think the most important thing about CETA is that it demonstrates that the question of what protections you have is a matter for negotiation and agreement, and therefore one can deal with concerns in that way. To my mind, the most important elements are, first, the definition of fair and equitable treatment. That can be quite a broad concept and you can legitimately ask what exactly that means in the hands of the body of arbitrators. CETA defines that quite carefully—at least, that is the intention behind it—so it would apply only if there was a denial of justice in criminal, civil or administrative procedures, a fundamental breach of due process or manifest arbitrariness: things of that sort. You would identify clearly what an absence of fair and equitable treatment is. It also, importantly, picks up the question of what is meant by the phrase “full protection and security”. That is quite a common phrase in investment treaties and it can be open to different interpretations. CETA says that that will apply only to the physical security of investors and investments and would not cover protection against changes in laws and regulations. That is the sort of thing that the negotiators could look at.

It also provides for some novel ideas in relation to the arbitral tribunals. That is less important in my view, but again there are things that could be looked at, such as both parties having to agree all the arbitrators. Normally both sides choose their own, subject to the obvious disqualification that they are then in place and the two will then choose the third arbitrator. It is suggested that a list should be agreed between the two parties—the EU and Canada—but that the arbitrator should be chosen by agreement. There are a number of features of that sort that are worth looking at when the negotiations take place.

**Q222 Baroness Coussins:** We have not seen the final text of CETA, of course, and I do not know whether anybody has, but we have been led to believe by earlier witnesses to this inquiry that it includes a new approach to this mechanism, including aspects such as binding arbitration, cost control, more transparency and a form of words that excludes legitimate

public policy areas. Dr Poulsen, if those innovations were also made part of TTIP, would they overcome your reluctance to accept that this kind of mechanism was important? Would they get rid of your concerns and criticisms?

**Dr Lauge Poulsen:** No.

**Baroness Coussins:** You would still be worried, even if there were all those things.

**Dr Lauge Poulsen:** The Commission has to be applauded for all the initiatives that it has taken in further clarifying the substantive standards that Lord Goldsmith spoke about and for useful language when it comes to the procedural provisions for the arbitration process, but that still does not go to the heart of the matter, which is why, when a Canadian investor runs into a dispute with the UK Government, that Canadian investor should not go through UK courts. I am not quite clear why a Canadian investor should have recourse to another adjudication mechanism when running into disputes with the UK Government that UK investors do not have. As I said before, the fundamental question of why foreign investors should have access to domestic courts that domestic investors do not have has not been answered by the European Commission. So while I agree that many of the provisions on the table in CETA are useful, they have not provided an answer to the fundamental question of why this is necessary in the first place when we talk about the protection of investment in the UK or the protection of investment in Canada.

**Lord Goldsmith:** That answer illustrates the real difference between us. I think that Dr Poulsen is a proponent of the Calvo doctrine, which is that if you invest in another state you have to subject yourself to the remedies of that state and nothing else. That is a legitimate point of view, but I think it is discredited today as a way to promote investment. People will not do that.

**Dr Lauge Poulsen:** I think I have to add to that comment. I have seen no evidence that the absence of an investment treaty with the United States means that UK investors are not

investing in the United States because of concerns about political risks. I have seen no evidence that US investors are investing less in the UK because of the absence of an investment protection agreement. I would challenge anyone who says that they have seen such evidence. I would very much like to see it. Secondly, I am not saying that there is no justification for an internationalised dispute settlement process if there has been a fundamental denial of justice in domestic courts, for instance. Then it makes sense. As we see in the European Court of Human Rights, you have to go through a domestic court first, then if something goes wrong you can take it to the international level, but in CETA Canadian investors do not even have to go through the UK courts. Now Lord Goldsmith is telling us that that will somehow mean that there will be less Canadian investment in the UK. I am not quite sure that that is the case.

**The Chairman:** Are we saying that we need better protection for our investments in the United States, and that therefore there is a price to pay for that?

**Dr Lauge Poulsen:** Again I am not sure, Lord Chairman, that UK investors need better protection in the United States than is already available in the United States.

**Lord Goldsmith:** Just do not go to Mississippi.

**Q223 Baroness Bonham-Carter of Yarnbury:** I think my question has already largely been dealt with. It goes back to CETA and whether it proves a useful precedent, which I think Lord Goldsmith has answered, but I will expand it a bit. Bearing in mind the difference between the EU and Canada in the US, as it were, do you think it is possible to negotiate a similar deal between the US and the EU to the CETA one? We know about the CETA one.

**Lord Goldsmith:** I am not party to or even close to the negotiations, or the pre-negotiations, that have taken place, so I have no idea where the differences may be. My fundamental point is that if one believes that it is right in general to have a system of protection but one is concerned about particular aspects of how that protection operates,

the right way to approach it is then to negotiate. I am not saying that CETA is necessarily absolutely right, but it illustrates the sort of things that one can do in negotiation, and this Committee can through its expert opinion guide the negotiators in a particular direction, which I think would be very valuable.

**Dr Lauge Poulsen:** The United States has traditionally been very hesitant about departing from its model bilateral investment treaty. Whether it is going to be the assessor in these negotiations is, again, not something that I am privy to. What is important, as I have highlighted before, is that the United States has historically been willing to exclude investment protection from its agreements, provided that there is no justification, as in the case of Australia, or in some other cases when the other party has tried to insist on provisions that depart from US treaty practice. One can speculate that if the EU is trying to use CETA as a precedent to negotiate with the United States, we could have a situation where ultimately the United States says, “We would rather have no agreement on investment protection than an agreement that follows the Commission’s proposals”. But, again, that is speculation.

**The Chairman:** Okay, well thank you both very much. We have come to a conclusion a little earlier than we had expected, but thank you both for the fullness of your replies and for the diversity of them from time to time.