Chapter 2

Issues

2.1 The Department of Foreign Affairs and Trade (DFAT) provides the following definition of ISDS provisions on its website:

> ISDS provisions grant foreign investors the right to access an international tribunal if they believe actions taken by a host government are in breach of commitments made in a Free Trade Agreement (FTA) or an investment treaty, thus providing additional protections for investors.[1]

2.2 Australia has negotiated ISDS provisions in free trade agreements signed over the past three decades. Currently, Australia has ISDS provisions in four free trade agreements: Australia-Chile Free Trade Agreement, Singapore-Australia Free Trade Agreement, Thailand-Australia Free Trade Agreement, ASEAN-Australia-New Zealand Free Trade Agreement. The Korea-Australia Free Trade Agreement, which has been signed but has not yet entered into force, also includes ISDS provisions.[2]

2.3 Australia currently has ISDS provisions in 21 bilateral investment treaties with Argentina, China, Czech Republic, Egypt, Hong Kong, Hungary, India, Indonesia, Laos, Lithuania, Mexico, Pakistan, Papua New Guinea, Peru, Philippines, Poland, Romania, Sri Lanka, Turkey, Uruguay and Vietnam.[3]

Australia US-Free Trade Agreement

2.4 The Senate Foreign Affairs, Defence and Trade References Committee conducted an inquiry into the Australia-United States (US) Free Trade Agreement in 2003. At the time, the committee noted that the inclusion of ISDS provisions in agreements with developing countries was a new development. These provisions had primarily been included in agreements to protect Australian investments and property from expropriation by governments in those countries where the rule of law was weak.[4]

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1 Department of Foreign Affairs and Trade, 'Frequently Asked Questions on Investor-State Dispute Settlement (ISDS)', https://www.dfat.gov.au/fta/isds-faq.html.

2 Department of Foreign Affairs and Trade, 'Frequently Asked Questions on Investor-State Dispute Settlement (ISDS)', https://www.dfat.gov.au/fta/isds-faq.html.

3 Department of Foreign Affairs and Trade, 'Frequently Asked Questions on Investor-State Dispute Settlement (ISDS)', https://www.dfat.gov.au/fta/isds-faq.html.

4 Foreign Affairs Defence and Trade References Committee, *Voting on Trade: The General Agreement on Trade in Services and an Australia –US Free Trade Agreement*, November 2003, p.134, http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Foreign_Affairs_Defence_and_Trade/Completed%20inquiries/2002-04/gats/report/index

2.5 The committee recommended that 'no investor-state provisions be included in the Australia-US Free Trade Agreement'. In the government response to the committee's report, DFAT stated that:

> The Investment Chapter of the AUSFTA does not establish an Investor State Dispute Settlement mechanism. This is in recognition of the Parties' open economic environments and shared legal traditions, and the confidence of investors in the fairness and integrity of their respective legal systems.[5]

Government policy

2.6 In April 2011, the Gillard government announced that it would no longer include ISDS provisions in free trade agreements. The new trade policy was announced in response to recommendations of the 2010 review of Bilateral and Regional Trade Agreements by the Productivity Commission.[6] The Gillard Government Free Trade Policy Statement stated that the government would not:

> …support provisions that would constrain the ability of Australian governments to make laws on social, environmental and economic matters in circumstances where those laws do not discriminate between domestic and foreign businesses. The Government has not and will not accept provisions that limit its capacity to put health warnings or plain packaging requirements on tobacco products or its ability to continue the Pharmaceutical Benefits Scheme.
>
> In the past, Australian Governments have sought the inclusion of investor-state dispute resolution procedures in trade agreements with developing countries at the behest of Australian businesses. The Gillard Government will discontinue this practice. If Australian businesses are concerned about sovereign risk in Australian trading partner countries, they will need to make their own assessments about whether they want to commit to investing in those countries.[7]

2.7 The Coalition government's position on current free trade agreement negotiations is that the inclusion of ISDS provisions will be considered on a case-by-case basis.[8]

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5 Department of Foreign Affairs and Trade, *Government response to the report of the Senate Foreign Affairs, Defence and Trade References–Voting on trade: The General Agreement on Trade in Services and an Australia-US Free Trade Agreement*, p. [12], http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Foreign_Affairs_Defence_and_Trade/Completed%20inquiries/2002-04/gats/index

6 Productivity Commission, Bilateral and Regional Trade Agreements, November 2010, http://www.pc.gov.au/__data/assets/pdf_file/0010/104203/trade-agreements-report.pdf

7 Department of Foreign Affairs and Trade, Gillard Government Trade Policy Statement: Trading our way to more jobs and prosperity, April 2011, p.14, http://www.acci.asn.au/getattachment/b9d3cfae-fc0c-4c2a-a3df-3f58228daf6d/Gillard-Government-Trade-Policy-Statement.aspx.

8 Department of Foreign Affairs and Trade, 'Frequently Asked Questions on Investor-State Dispute Settlement (ISDS)', https://www.dfat.gov.au/fta/isds-faq.html.

Tobacco plain packaging—investor-state arbitration

2.8 To date, Australia has had one investor-state dispute claim brought against it. The *Tobacco Plain Packaging Act 2011* forms part of a comprehensive range of tobacco control measures designed to reduce the rate of smoking in Australia. Phillip Morris Asia is challenging the tobacco plain packaging legislation under the 1993 Agreement between the Government of Australia and the Government of Hong Kong for the Promotion and Protection of Investments (Hong Kong Agreement). The Attorney-General's Department summarised Phillip Morris Asia's arguments:

> Philip Morris Asia is arguing that Australia's tobacco plain packaging measure constitutes an expropriation of its Australian investments in breach of Article 6 of the Hong Kong Agreement. Philip Morris Asia further argues that Australia's tobacco plain packaging measure is in breach of its commitment under Article 2(2) of the Hong Kong Agreement to accord fair and equitable treatment to Philip Morris Asia's investments. Philip Morris Asia further asserts that tobacco plain packaging constitutes an unreasonable and discriminatory measure and that Philip Morris Asia's investments have been deprived of full protection and security in breach of Article 2(2) of the Hong Kong Agreement. Australia rejects these claims.[9]

2.9 The case has been brought before the World Trade Organisation's (WTO) dispute settlement system.[10]

Arguments in support the bill

2.10 The majority of submissions received by the committee supported the intention of the bill, based on concerns about the risks associated with the inclusion of ISDS provisions in trade agreements. These were captured in evidence from Dr Tienhaara at the inquiry's public hearing:

> In recent years the Australian public has become increasingly aware of the shortcomings of ISDS and the risk that it poses to public policy, particularly since the launch of the case against plain packaging by Philip Morris….[A]ccording to UNCTAD, by the end of 2013, 98 states had been respondents in a total of 568 known treaty based cases. Argentina has faced 53 ISDS cases, Canada 22 and the United States 15. The vast majority of ISDS cases—about 75 per cent—are brought by American and European investors.

2.11 Other submitters raised concerns over the significant growth in the number of ISDS cases being brought internationally in recent years. The Australian Fair Trade and Investment Network (AFTINET), a network of 60 community organisations, noted that the number of known ISDS cases lodged each year has increased from less

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9 Attorney-General's Department, 'Tobacco plain packaging—investor-state arbitration', http://www.ag.gov.au/Internationalrelations/InternationalLaw/Pages/Tobaccoplainpackaging.aspx

10 Attorney-General's Department, 'Tobacco plain packaging—investor-state arbitration', http://www.ag.gov.au/Internationalrelations/InternationalLaw/Pages/Tobaccoplainpackaging.aspx

than five in 1993 to 57 in 2013.[11] Dr Patricia Ranald outlined the concerns of AFTINET:

> ISDS basically gives additional special rights to foreign investors to sue governments for damages in an international tribunal on the basis of a claim that domestic legislation or policy has harmed their investment. It has developed from a system that originally was about compensating for the actual expropriation of property—real property. But over the years, particularly the last 20 years, it has developed into a system based on principles of indirect expropriation that simply do not exist in most legal systems and that are not available to domestic investors. In that sense it is not about free trade; it is about giving special preferential treatment to foreign investors compared with domestic investors.[12]

2.12 The implications of the Phillip Morris plain packaging case against Australia and similar cases that have been brought against other countries were also an area of concern. Dr Rimmer explained that:

> A really important theme in Australia, Canada, the United States and the European Union has been the way in which corporations have tried to deploy investor clauses to challenge decisions of superior courts.
>
> …
>
> That is a really critical issue. Think about the battle over plain packaging of tobacco products in Australia, where you had the High Court of Australia very decisively—six to one—ruling in favour of the Commonwealth government against the big tobacco companies and then Philip Morris trying to attack plain packaging through an investment clause.[13]

2.13 According to Dr Rimmer, the other important theme is the impact of ISDS upon the role of governments. He explained that:

> There has been a lot of concern about the chilling impact of investor-state dispute settlement upon public regulation and government activity, and it has been particularly prominent with the rise and rise of disputes in relation to investor-state dispute settlement.[14]

2.14 Submissions supporting the bill expressed concerns about a wide range of policy areas which could potentially be subject to ISDS claims, or threats of ISDS claims, which may impact on the government's ability to regulate. For example:

- the New South Wales Teachers Federation expressed concern that government may face ISDS claims from private education providers which may impact on the provision of public education in the future;[15]

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11 Australian Fair Trade and Investment Network (AFTINET), *Submission 105*, p. 7.

12 Dr Patricia Ranald, Australian Fair Trade and Investment Network (AFTINET), *Committee Hansard*, 6 August 2014, p. 29.

13 Dr Matthew Rimmer, *Committee Hansard*, 6 August 2014, p. 7.

14 Dr Matthew Rimmer, *Committee Hansard*, 6 August 2014, p. 7.

15 New South Wales Teachers Federation, *Submission 42*, pp. 2–4.

- a number of submitters were concerned that the Pharmaceutical Benefits Scheme may be under threat which could limit access to affordable medicines,[16] in particular the potential impacts on the health of Aboriginal and Torres Strait Islander people;[17]
- concerns were also raised about ability of future governments to regulate to protect the environment in areas such as mining permits, promoting renewable energy and restricting coal seam gas (CSG) exploration and extraction;[18] and
- in light of the cigarette plain packaging case, submitters were also concerned about the impact on other public health policies.[19]

2.15 Evidence received from Mrs Tracey Tipping expressed the types of concerns raised by individuals and organisations. Mrs Tipping told the committee that after undertaking her own research she was so concerned about the effects of ISDS provisions that she initiated a community petition to ban the provisions in all future trade agreements, which received over 9000 signatures. Mrs Tipping runs an online business specialising in organic and eco-friendly products. Her areas of concern included the possible impact of ISDS provisions on the Tasmanian government's moratorium on genetically modified organisms (GMOs), and the effect on food labelling legislation.[20]

> I think it is really important for Tasmania in terms of its overall brand as a clean, green state. I personally think the jury is still out on genetically engineered organisms and that there is nothing wrong with states wanting to have a moratorium or ban in place. I think they should have that opportunity. If they had then put in a moratorium after the ISDS provisions, they would have most likely faced a lawsuit. I think, particularly, for a small state like Tasmania, with a $250 million lawsuit, you would abandon your policy straightaway. I can see it is a pretty tough economy over there. I can't see them persevering with a policy that they feel has merit but could involve a major lawsuit.[21]

16 See for example: Professor Thomas Faunce, Australian National University, *Submission 49*, pp. 22–27; New South Wales Nurses and Midwives' Association, *Submission 67*, p. 2; Médicins Sans Frontières, *Submission 89*, pp. 3–5.

17 Mr Terry Mason, Indigenous Policy Committee, National Tertiary Education Union, *Submission 103*, p. 1.

18 See for example: 350.org, Submission 75, pp. [3–5]; Safe Climate Brisbane, *Submission 96*, p. [2].

19 See for example: New South Wales Nurses and Midwives' Association, *Submission 67*, p. 3; Australian Medical Students' Association, Submission 80, p. 2; Public Health Association of Australia (PHAA), *Submission 91*, pp. 4–5

20 Mrs Tracey Tipping, Eternal Source PTY LTD, *Committee Hansard*, 6 August 2014, pp.1–2; GM Free Australia Alliance Inc also raised concerns regarding GMOs, *Submission 29*, p. [2].

21 Mrs Tracey Tipping, Eternal Source PTY LTD, *Committee Hansard*, 6 August 2014, p. 2.

Other issues raised in evidence

2.16 A number of submitters raised a set of broader issues regarding the inclusion of ISDS provisions in trade agreements which the committee considers important to note. These focus on regulatory chill, the effectiveness of safeguards, ISDS and developing countries, transparency, parliamentary scrutiny, and international reviews of ISDS. These are discussed below.

Regulatory Chill

2.17 AFTINET argued that the increase in the number and type of ISDS claims brought against governments has led to an effect known as 'regulatory chill'.

> This is a situation in which governments are made aware of the threat and costs of both protracted litigation and damages, and are discouraged from legitimate regulation because of these threats.[22]

2.18 Dr Tienhaara explained in her submission that:

> The concept of regulatory chill reflects the fact that policy makers will be wary of introducing measures that could be challenged in arbitration because of the immense costs associated with the arbitration system and the uncertainty surrounding how investment provisions will be interpreted in any given case. Occurrences of regulatory chill are incredibly difficult to prove (effectively one has to find evidence of something that hasn't happened). Nevertheless, several scholars have put forward case studies that suggest that investor threats of arbitration had an impact on the development of specific policies.[23]

2.19 Professor Weatherall informed the committee that there were number of examples in the area of intellectual property where 'specific obligations that have been negotiated in these free trade agreements have been cited as reasons not to do law reforms that might otherwise be desirable'.[24]

2.20 In their submission, Dr Sam Luttrell and Dr Romesh Weeramantry noted that:

> Empirical evidence for the phenomenon is, however, still lacking. But that does not mean it should be dismissed, only that more work needs to be done before regulatory chill can be considered a reliable policy premise.[25]

2.21 Professor Nottage agreed that further empirical testing was necessary. He also argued that Australia, and other developed countries, are already subjected to regulatory chill because:

> …our courts are full of cases where concerned citizens and corporations are challenging government action or inaction through our court system. We are also subject to regulatory chill from interstate dispute settlement

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22 Australian Fair Trade and Investment Network (AFTINET), *Submission 105*, p. 4.

23 Dr Kyla Tienhaara, RegNet/College of Asia and the Pacific, Australian National University, *Submission 86*, p. 20.

24 Associate Professor Kimberlee Weatherill, *Committee Hansard*, 6 August 2014, p. 28.

25 Dr Sam Luttrell and Dr Romesh Weeramantry, *Submission 106*, p. 6.

> processes, including the WTO claims, including in relation to investment in services sectors under the General Agreement on Trade in Services—GATS. So, especially in developed countries, the extra regulatory chill could well be overstated. But, again, it is a matter that needs to be tested.[26]

Safeguards

2.22 Professor Weatherall noted in her submission that recent trade agreements have included safeguards designed to 'confine investor claims and in particular to ensure that legitimate regulation in the public interest does not give rise to a claim for compensation'.[27]

2.23 In her submission, Professor Emerita Dorothy Broom AM argued that:

> Promised 'carve outs' are a start, but they cannot possibly protect Australians from the harm that can arise from ISDS since they cannot anticipate the diverse grounds on which an investor might complain in the future.[28]

2.24 The National Tertiary Education Union argued that if future Australian governments enter into agreement including ISDS provisions:

> …it is fundamental that precise and detailed language circumscribing the meaning of key phrases such as 'expropriation', 'investor' and 'investment' is included to prevent cases that penalise governments for introducing legislation with public welfare objectives.[29]

2.25 Professor Weatherall pointed out that while there are ways to limit investor-state dispute claims, 'the question really is whether those ways are being inserted into the Australian negotiated agreements'.[30]

2.26 Professor Weatherall gave evidence to the committee comparing the Canada-Korea Free Trade Agreement to the Korea-Australia Free Trade Agreement, both of these agreements were concluded in 2014. Professor Weatherall noted that carve-outs and safeguards are significantly stronger in the Canada-Korea agreement. She advised the committee that:

> …the definition of expropriation is narrower [in the Canada-Korea agreement], particularly where you are talking about expropriation that occurs through indirect regulatory means. The intellectual property carve-out is better in the Korea-Canada agreement, because it refers to the TRIPS standards, which are more flexible than the specific IP chapter standards. The general regulatory exclusion in the expropriation annex is also wider, or better for allowing some regulatory freedom for the state in the Korea-

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26 Professor Luke Nottage, *Committee Hansard*, 6 August 2014, p. 28.

27 Associate Professor Kimberlee Weatherall, Sydney Law School, University of Sydney, *Submission 88*, p. 6.

28 Professor Emerita Dorothy Broom AM, *Submission 35*, p. [3].

29 National Tertiary Education Union, *Submission 129*, pp. 9–10.

30 Associate Professor Kimberlee Weatherall, *Committee Hansard*, 6 August 2014, p. 23.

> Canada agreement…I do think that the Canada agreement is a salutary comparison with the Australian one. I think it suggests that the safeguards are not the latest safeguards or the strongest safeguards that are available in international law.[31]

2.27 Professor Weatherall noted that while the safeguards that have been included in KAFTA for example, are an improvement on the language in older agreements. However, as they are drafted, they may not prevent claims being brought, although they may reduce the likelihood of success.[32]

2.28 Professor Nottage put the case for Australia to look into developing its own model international investment treaty, as is the practice of many of our trading partners, in both developed and developing countries.[33] He argued that:

> … there would be a lot of benefit in more structured public discussion led by the government about not only investor-state dispute settlement but also the broader international investment treaty regime, including the substantive rights…[34]

2.29 Professor Weatherall also raised concerns that the particular wording in the KAFTA agreement may have the undesirable effect of making the intellectual property chapter a direct subject of arbitration.[35]

2.30 In response to these concerns, Mr Braddock, DFAT stated:

> At least in terms of Australia's experience with investment agreements and ISDS, that is not the case. ISDS applies only to investment obligations; it does not apply to obligations in other chapters.[36]

Developing Countries

2.31 Some submitters expressed concern about the potential negative effect of ISDS provisions in trade agreements with developing countries. In support of the bill, AID/WATCH argued that:

> ISDS provisions have no place in Australian trade agreements not only for the important reason of protecting Australia's law and policy, but also because ISDS disproportionately disadvantages developing countries who don't have equal resources to defend cases and provisions.[37]

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31 Associate Professor Kimberlee Weatherall, *Committee Hansard*, 6 August 2014, p. 24.

32 Associate Professor Kimberlee Weatherall, Sydney Law School, University of Sydney, *Submission 88*, p. 7.

33 Professor Luke Nottage, Sydney Law School, University of Sydney, *Submission 21*, p. 5.

34 Professor Luke Nottage, *Committee Hansard*, 6 August 2014, p. 27.

35 Associate Professor Kimberlee Weatherall, Sydney Law School, University of Sydney, *Submission 88*, p. 7.

36 Mr Richard Braddock, Department of Foreign Affairs and Trade, *Committee Hansard*, 6 August 2014, p. 45.

37 AID/WATCH, *Submission 107*, p. 1; see also Dr Kyla Tienhaara, RegNet/College of Asia and the Pacific, Australian National University, *Submission 86*, p. 27.

2.32 Dr Tienhaara argued that regulatory chill is more likely to occur in developing countries due to the significant costs of arbitration.[38]

2.33 Professor Nottage noted that:

> The treaty-based ISDS system is particularly important when dealing with developing countries, where local courts and substantive rights may not meet widely-accepted global standards, although ISDS is also now found in some treaties among developed countries.[39]

Transparency

2.34 While Dr Hazel Moir supported the bill, she reasoned that if ISDS provisions are to be included in trade agreements, then minimum requirements should be set for arbitrations mechanisms. Dr Moir recommended that:

- all proceedings are public;
- judges are independent; and
- there should be a further appeal mechanism.[40]

2.35 Dr Tienhaara noted that there had been some advances in the transparency of arbitration proceedings in recent years. For example, the members of the United Nations Commission on International Law (UNCITRAL) developed a special set of rules regarding transparency that will apply to all agreements using UNCITRAL Rules that are signed after 1 April 2014. Dr Tienhaara explained that this will have limited impact however, as:

> …as most treaties allow investors to choose between different sets of rules, adoption of the new UNCITRAL transparency standards cannot be guaranteed and it remains the case that under the ICSID Rules hearings are not opened to the public unless both parties agree. Investors have opted for closed hearings in several recent cases concerning public policy. To avoid this problem, strong provisions on transparency must also be included in the text of IIAs [International Investment Agreements], but this requires that all negotiating parties agree that transparency is important.[41]

2.36 Professor Nottage commented on the concern in Australia and other developed countries to enhance the transparency of proceedings. His view was that:

> I predict that the EU and the US will retain ISDS in some form but certainly with enhanced transparency, which they have already started to introduce in some of their treaties, which will take them perhaps to the next level. I think

38 Dr Kyla Tienhaara, RegNet/College of Asia and the Pacific, Australian National University, *Submission 86*, p. 27.

39 Professor Luke Nottage, Sydney Law School, University of Sydney, *Submission 21*, p. 2.

40 Dr Hazel Moir, Adjunct Associate Professor, Research School of Social Sciences, Australian National University, *Submission 56*, p. 2.

41 Dr Kyla Tienhaara, RegNet/College of Asia and the Pacific, Australian National University, *Submission 86*, p. 7.

> that is the sort of thing Australia should be engaging in and doing as well, rather than just getting rid of ISDS completely, as proposed in this bill.[42]

Parliamentary scrutiny

2.37 Many submitters expressed concerns about the lack of transparency in trade negotiations in general, as well as in relation to ISDS provisions. Of particular concern was the secrecy surrounding the Trans-Pacific Partnership (TPP) agreement which is currently being negotiated.[43]

2.38 The National Tertiary Education Union argued that if the government does intend to continue its policy of including ISDS provisions on a case-by-case basis it has 'in the least an obligation to publicly specify the contexts and each rationale in which ISDS will be negotiated on behalf of the Australian people'.[44]

2.39 The Australia Institute submission raised concerns about the transparency of trade negotiations and, in its view the limited capacity for parliamentary oversight and scrutiny. The Australia Institute noted that the Joint Standing Committee on Treaties only get the opportunity to review trade agreements after the text has already been agreed upon by negotiating parties and cabinet. The Australia Institute is also concerned that the time allocated for parliamentary scrutiny by the Joint Standing Committee on Treaties (JSCOT) is inadequate given the scale and complexity of trade agreements.[45]

2.40 The Law Council of Australia suggested that a system, which would:

> …provide opportunities for stakeholders to provide an input into preferential trade agreements before they actually go before parliament or before cabinet so that there is an input and that they actually review them and ask: is this actually in the national interest? Is there a benefit?
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> …
>
> I think there needs to be some more formal input by stakeholders. I know that the Department of Foreign Affairs and Trade does have consultations with stakeholders. I suggest that is probably largely ad hoc. But it will be useful for parliament to actually have industry groups reviewing particular agreements and asking: is this or is this not in the national interest?[46]

2.41 Dr Ranald, AFTINET agreed that greater scrutiny of agreements before they go to parliament would be beneficial:

> Certainly we would prefer to have a situation, as occurs in the WTO, actually, where draft texts are made available for public discussion. In our opinion that would ensure a better result at the end, because it allows a full

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42 Professor Luke Nottage, *Committee Hansard*, 6 August 2014, p. 28.

43 See for example; Lock the Gate Alliance, *Submission 133*, p. 4.

44 National Tertiary Education Union, *Submission 129*, p. 9.

45 The Australia Institute, *Submission 79*, p. 5.

46 Mr Andrew Percival, Law Council of Australia, *Committee Hansard*, 6 August 2014, p. 34.

> range of opinions, ranging from that of the chamber of commerce to AFTINET's, to have an impact on the negotiations before decisions are made.[47]

International reviews

2.42 A number of submitters drew the committee's attention to the public consultation process which has been instituted by the European Commission to provide an opportunity for public examination and debate following widespread protests against ISDS in Europe in the context of the Trans-Atlantic Trade and Investment Partnership (TTIP) negotiations.[48]

2.43 Submitters also noted that other countries, including France, Germany, South Africa, Argentina and Brazil have been reassessing ISDS provisions.[49]

2.44 Professor Nottage argued that rather than introducing a blanket probation on the inclusion of ISDS provisions:

> It is more responsible therefore for Australia to keep engaging with the system by negotiating specific improvements in future treaties. This is also the approach taken recently by the European Commission and US government, which have been reassessing ISDS as well.[50]

Arguments against the bill

2.45 A number of submitters provided compelling arguments as to why the bill should not be supported. Professor Nottage told the committee that although he thought the bill was well-intentioned, in the sense that the ISDS treaty-based system is far from perfect, he could not support the bill because:

> [it] would make Australia unique among developed countries and put us in the company of a very few countries, even among developing countries, mainly a few very Leftists regimes in South America. I think it would torpedo future trade and investment treaty negotiations to which the major parties in Australia have long been committed, as well as potentially inhibit the development of multilateral initiatives and international investment law.[51]

2.46 In its submission, DFAT argued that the bill may prevent the Government from concluding negotiations to benefit Australian producers, consumers, investors and the broader community. Furthermore, excluding ISDS provisions from future trade agreements would impose a significant limitation on the ability of the

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47 Dr Patricia Ranald, AFTINET, *Committee Hansard*, 6 August 2014, p. 32.

48 See for example: IndutriALL Global Union, *Submission 20*, p. 2; Centre for Health Equity Training, Research and Evaluation (CHETRE), *Submission 66*, p. 4. Australian Council of Trade Unions, *Submission 81*, p. 10.

49 See for example: IndutriALL Global Union, *Submission 20*, p. 2; Australian Council of Trade Unions, *Submission 81*, pp. 9–10.

50 Professor Luke Nottage, Sydney Law School, University of Sydney, *Submission 21*, p. 3.

51 Professor Luke Nottage, *Committee Hansard*, 6 August 2014, p. 20.

Government to pursue its broader trade and investment objectives. DFAT noted that the bill is inconsistent with the Government's policy to consider the inclusion of ISDS provisions in trade agreements on a case-by-case basis.[52]

Australian Investors

2.47 Dr Sam Luttrell and Dr Romesh Weeramantry argued in their submission that even though Australia has low sovereign risk and reliable courts, it should not reject the inclusion of ISDS clauses. They note that:

> ISDS provisions are typically intended to protect investors doing business in countries with high sovereign risk. Where a treaty is signed between two countries that both have similar and low sovereign risk, the negotiators may not consider it necessary to include an ISDS clause. This is why, for example, the United States-Australia Free Trade Agreement does not include an ISDS clause. But this parity of sovereign risk is relatively rare. The far more common scenario is one in which there is a significant disparity in the sovereign risk of the states that are negotiating the treaty. In this situation, the low sovereign risk state will have a strong interest in obtaining ISDS protection for its nationals when they invest in the high sovereign risk state. To secure that essential protection for its investors, it will almost always be necessary for the low sovereign risk state to agree to a reciprocal ISDS clause, i.e. an ISDS clause that allows both contracting states to be sued, not just the high sovereign risk state.[53]

2.48 Mr De Cure, First Assistant Secretary, DFAT, advised the committee that major Australian companies and businesses, with significant investments overseas support the inclusion of ISDS provisions such as, the Business Council of Australia, the Chamber of Commerce and Industry, BHP, Rio Tinto.[54]

2.49 The Australian Chamber of Commerce and Industry expressed concern that although Australian investors have not utilised ISDS provisions to any great extent in the past, if a ban on ISDS provisions was implemented it would prevent Australian firms from being able to protect their international interests by using such provisions.[55] The Australian Dental Industry Association noted similar concerns in the dental industry.[56]

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52 Department of Foreign Affairs and Trade, *Submission 135*, p. 1.

53 Dr Sam Luttrell and Dr Romesh Weeramantry, *Submission 106*, pp. 2–3.

54 Mr Chris De Cure, Department of Foreign Affairs and Trade, *Committee Hansard*, 6 August 2014, p. 45.

55 Australian Chamber of Commerce and Industry, *Submission 105*, p. 5.

56 Australian Dental Industry Association , *Submission 122*, p. 3.

Wording of the bill

2.50 DFAT maintained that the bill fails to recognise that safeguards can be incorporated in ISDS provisions to protect the public interest.[57] Mr De Cure explained:

> In particular, more recent agreements…contain considerably more explicit safeguards than were contained in some of the earlier agreements. These safeguards have been developed in response to concerns about challenges to legitimate public welfare regulation. ISDS does not prevent governments from changing their policies or regulating in the public interest and we do not believe that it freezes existing policy settings. ISDS does not entitle investors to compensation just because they object to a government policy or because it affects their profits.[58]

2.51 DFAT also noted that the bill would prevent the government from seeking to update agreements containing ISDS in the future. In its submission, the department explained that:

> DFAT considers that the Bill may have unintended consequences which would not serve the interests it is purportedly seeking to address. In particular, the Bill would prevent the Government from seeking to update agreements containing ISDS should it wish to do so in the future, for example to include more explicit safeguards for public welfare regulation.[59]

2.52 Professor Nottage noted that there are other alternatives to manage the risks associated with ISDS more effectively, which do not require legislation such as seeking to improve the drafting of old treaties. [60] In particular, redrafting treaties such as the one with Hong Kong which was concluded in the early 1990s, which is the treaty that has led to the first ISDS claim being brought against the Australian government by Phillip Morris.[61]

2.53 DFAT argued further, the wording of the bill would exclude Australia from entering a plurilateral agreement which includes ISDS, regardless of whether Australia agrees to be bound by that particular provision.[62] Mr De Cure, First Assistant Secretary, DFAT told the committee the Trans-Pacific Partnership Agreement would be an example of an instance in which the bill might preclude the Australian government from participating in negotiations.[63]

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57 Department of Foreign Affairs and Trade, *Submission 135*, p. 2.

58 Mr Chris De Cure, Department of Foreign Affairs and Trade, *Committee Hansard*, 6 August 2014, p. 42.

59 Department of Foreign Affairs and Trade, *Submission 135*, p. 2.

60 Professor Luke Nottage, Sydney Law School, University of Sydney, *Submission 21*, p. 5.

61 Professor Luke Nottage, *Committee Hansard*, 6 August 2014, p. 20.

62 Department of Foreign Affairs and Trade, *Submission 135*, p. 2.

63 Mr Chris De Cure, Department of Foreign Affairs and Trade, *Committee Hansard*, 6 August 2014, p. 49.

2.54 Mr Percival from the Law Council of Australia agreed with this assessment:

> So if there was an agreement such as a bilateral investment treaty which included an ISD provision and there was a proposed amendment to it, [the bill] would prohibit that amendment. Whether that is a good or bad thing would depend, in my view, and should be assessed on its merits, not as a blanket prohibition. It would depend on what the amendment was—it may have actually nothing to do with the ISD provision at all.[64]

2.55 Professor Nottage observed that the bill appears to be aimed at reinstating the April 2011 'Gillard Government Trade Policy Statement'. He argued that the bill and the 2011 Gillard Government trade policy:

> …may be well-intentioned, but it is **premature and misguided. Treaty-based ISDS is not a perfect system, but it can be improved in other ways** [emphasis in original] – mainly by carefully negotiating and drafting bilateral investment treaties (BITs) and free trade agreements (FTAs) This may also have the long-term benefit of generating a well-balanced new investment treaty at the multilateral level, which is presently missing and unlikely otherwise to eventuate.[65]

2.56 The Law Council of Australia argued that there is no case for a blanket prohibition, such as that proposed by the bill. The Law Council argues that consideration of the inclusion of an ISDS provision in an agreement should be examined on a case-by-case basis. In its submission, the Law Council of Australia noted that:

> …exceptions to ISDS provisions can be provided similar to the exceptions in Article XX of the General Agreement on Tariffs and Trade 1947 (such as, exceptions for the protection of human and animal health and welfare, the environment, public morals.) For example, investment treaties concluded by Australia, such as the Free Trade Agreement with Chile and the Free Trade Agreement with Korea, include provisions providing various safeguards to protect various public interests, including transparency of proceedings, while retaining ISDS provisions.[66]

Committee View

2.57 The committee understands the intention of the bill and notes that it has generated much public discussion regarding the inclusion of ISDS provisions in existing and new trade agreements. The committee also acknowledges the arguments put by those who made submissions to the inquiry and is encouraged by the interest shown by organisations and individuals working in this area.

2.58 The committee draws to DFAT's attention the submissions received during the inquiry. The committee sees benefit in the government giving further

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64 Mr Andrew Percival, Law Council of Australia, *Committee Hansard*, 6 August 2014, p. 35.

65 Professor Luke Nottage, Sydney Law School, University of Sydney, *Submission 21*, pp.1–2.

66 Law Council of Australia, *Submission 90*, pp. 1–2.

consideration to the issues raised in the submissions regarding the inclusion of ISDS provisions in free trade negotiations and the potential effects on Australian business.

2.59 On balance the committee is not convinced that legislation is the best mechanism by which to address the concerns raised about risks associated with ISDS provisions. The committee agrees with Professor Nottage and others that the risks associated with ISDS can and should be managed more effectively and in ways which do not require legislation, including careful treaty drafting (of both old and new agreements) and development of a well-balanced Model Investment Treaty.[67]

2.60 The committee is of the view that many of the alleged risks to Australian sovereignty and law making arising from the ISDS system are overstated and are not supported by the history of Australia's involvement in negotiating trade agreements. While the committee acknowledges that past experience may not be an accurate guide to the future in terms of potential ISDS claims against Australia, it stresses that the investment treaty arbitration field is evolving in positive ways to enable countries, including Australia, to put exclusions in place, limit the application of ISDS to the investment sections of agreements, and generally tighten up the wording of agreements. The committee is of the view that it is far more important for Australia to manage any risks associated with ISDS provisions than to reverse its longstanding treaty practice and opt out of the ISDS system altogether.

2.61 The committee accepts the view that the ISDS system has improved significantly over recent years both in the way treaties are drafted in relation to ISDS clauses and in the way that cases are argued and how arbitrators decide cases. Australia therefore stands to gain more by remaining actively engaged with the international investment law system, including where ISDS provisions apply. The committee is concerned that were Australia to legislate for a blanket ban on ISDS provisions in trade agreements, it would be sending a message to existing and potentially new trading partners that Australia was turning inward-looking and distancing itself from the international law system.

2.62 The committee is of the view that a blanket ban on ISDS would impose a significant constraint on the ability of Australian governments to negotiate trade agreements that benefit Australian business. It is for this reason that the committee considers the current case-by-case approach to ISDS is in Australia's long-tern national interest and a sound policy for weighing the risks and benefits of ISDS provisions in trade agreements.

Recommendation

The committee recommends that the bill not be passed.

Senator Chris Back
Chair

67 Professor Luke Nottage, Sydney Law School, University of Sydney, *Submission 21*, p. 5.