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SYMPOSIUM ON SERGIO PUIG AND GREGORY SHAFFER, "IMPERFECT ALTERNATIVES: INSTITUTIONAL CHOICE AND THE REFORM OF INVESTMENT LAW," AND ANTHEA ROBERTS, "INCREMENTAL, SYSTEMIC, AND PARADIGMATIC REFORM OF INVESTOR-STATE ARBITRATION"

A TRINITY ANALYTICAL FRAMEWORK FOR ISDS REFORM

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The *American Journal of International Law*'s recent articles on the reform of investor-state dispute settlement (ISDS) make important contributions to ongoing debates. The article by Sergio Puig and Gregory Shaffer elaborates on the *methods* of investment dispute resolution—the various institutional innovations that states might pursue to improve the system.[1] The essay by Anthea Roberts in turn explores the *subjects* of investment dispute resolution—states and their varying positions on reform.[2] In our essay, we supply a third perspective by discussing the *objects* of ISDS—that is, the disputes themselves, which vary considerably from one case to another. We believe that considering methods, subjects, and objects together—what we refer to as a "trinity analytical framework"—could assist states as they formulate their positions in the reform process going forward. At the same time, we do not think that all reform options are equally meritorious, and we critique Puig and Shaffer's proposal for complementarity between municipal courts and international mechanisms as at best premature.

A Trinity Analytical Framework: Methods, Subjects, and Objects of Investment Dispute Settlement

Puig and Shaffer's *Imperfect Alternatives: Institutional Choice and the Reform of Investment Law*[3] focuses on comparative analysis of the six main types of institutional alternatives to international investment dispute settlement by evaluating the trade-offs among them in relation to the goals of investment law. Since every institutional alternative is imperfect, the article contends that state's choices should be made in context. By focusing on the merits of options such as an investment court and mediation, the authors approach the question of ISDS reform primarily from the perspective of the "methods" of investment dispute resolution.

In contrast, Roberts focuses on states—the "subjects" of ISDS—by categorizing them as seeking either *incremental*, *systemic*, or *paradigmatic* reform.[4] She identifies the likely strategies of and risks faced by the different reform

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[1] Sergio Puig & Gregory Shaffer, *Imperfect Alternatives: Institutional Choice and the Reform of Investment Law*, 112 AJIL 361 (2018).

[2] Anthea Roberts, *Incremental, Systemic, and Paradigmatic Reform of Investor-State Arbitration*, 112 AJIL 410 (2018).

[3] Puig & Shaffer, *supra* note 1.

[4] Roberts, *supra* note 2.

champions, and then assesses the role of the UN Commission on International Trade Law (UNCITRAL) as both a venue and an actor in ISDS reform. In the end, Roberts predicts a pluralistic outcome featuring multiple, coexisting approaches and offers several suggestions as states proceed with reform. This work is not inconsistent with Puig and Shaffer's analysis; rather, it tackles the issue of ISDS reform from a different angle.

Both papers, however, fail to address a third important aspect of the ISDS mechanism—the *objects* of dispute resolution, namely the disputes per se. Investment disputes constitute the foundation of the system of investment dispute resolution. Without understanding them, it is impossible to fully appreciate the ISDS mechanism, let alone improve upon it. This is particularly true given the complexity involved in investor-state disputes. Unlike straightforward state-to-state or commercial disputes, investor-state claims are "mixed" in that they involve a sovereign state (a public body) on the one hand and a foreign investor (a private body) on the other. As a result, investor-state disputes give rise to special demands that cannot be met through ordinary commercial arbitration or state-to-state settlement procedures. Indeed, this is why states have created special mechanisms, such as International Centre for Settlement of Investment Disputes arbitration, for mixed disputes.

A matrix analytical framework (MAF)[5] offers a useful tool to more closely examine the various forms of investment disputes, as well as the different methods that should be used to resolve them. In so doing, the framework fills a gap left by the works of Puig and Shaffer, Roberts, and the literature on ISDS reform as a whole. In practical terms, states would first employ the MAF in considering the types of investment disputes to be covered by their investment treaties. Then they would apply the comparative institutional analysis proposed by Puig and Shaffer to consider the international and domestic dispute-settlement mechanisms that might be suitable for those disputes. Finally, they would assess their options and decide which of the camps of ISDS reformers to join, including in multilateral fora such as UNCITRAL, the Organization for Economic Cooperation and Development, and the World Trade Organization. In other words, the MAF, together with the analytical frameworks provided by Puig, Shaffer, and Roberts, would be consolidated as a three-in-one or trinity analytical framework.

The Matrix Analytical Framework

It is beyond doubt that every investment dispute involves certain economic interests and therefore has an economic dimension. But unlike ordinary commercial disputes, investment disputes often involve interests that go beyond the economic sphere and implicate political and social issues as well. This is because, as mentioned above, investment disputes tend to involve both public and private bodies and interests. The involvement of public interests often implies that the disputes carry certain political implications. For example, ISDS tribunals must at times assess whether taxation measures (such as the "windfall tax" bill of Ecuador[6]) or measures taken in response to financial crisis in the host state (such as in Argentina[7]) violate state obligations under the applicable investment treaty. In addition, foreign investment—particularly foreign direct investment—often involves frequent interactions with the local communities of receiving states in ways that trigger social attention and concern. The Philip Morris case, in which the tobacco company accused Australia of breaching investment treaty obligations by

[5] One of us first proposed the matrix analytical framework in a presentation at the 24th Energy Charter Ministerial Conference, held in Cyprus. *See* Wenhua Shan, A Matrix Analysis on ISDS Reform: Preliminary Considerations (Dec. 2013). An article developed on the basis of this presentation is forthcoming. *See* Wenhua Shan & Peng Wang, *A Matrix Analytical Framework for Investment Disputes and Their Settlement*, 33 ICSID Rev. (forthcoming 2018).

[6] *See, e.g.*, Burlington Res., Inc. v. Ecuador, ICSID Case No. ARB/08/5; Murphy Exploration & Prod. Co. Int'l v. Ecuador, ICSID Case No. ARB/08/4.

[7] *See, e.g.*, CMS Gas Transmission Co. v. Arg., ICSID Case No. ARB/01/8; Azurix Corp. v. Arg. (I), ICSID Case No. ARB/01/12; Siemens A.G. v. Arg., ICSID Case No. ARB/02/8.

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Table 1: Simplified Categorization of Investment Disputes

	High Political Sensitivity	Low Political Sensitivity
High Social Sensitivity	Red Zone(both politically and socially sensitive disputes)	Blue Zone(socially but not politically sensitive disputes)
Low Social Sensitivity	Yellow Zone(politically but not socially sensitive disputes)	Green Zone(both politically and socially insensitive disputes)

adopting a "plain packaging bill," is illustrative.[8] Although the political and social dimensions of investment disputes can be distinguished from each other, they are often interlinked and intertwined, particularly in Western democracies. The presence and at times the compound effect of these noneconomic dimensions make investment disputes much more complex than ordinary commercial or state-to-state disputes.

The MAF is helpful because it helps to illuminate these dimensions. Considering them together, we can categorize investment disputes as falling into any of four zones: the Green Zone, the Red Zone, the Yellow Zone, or the Blue Zone. Table 1 places these zones into a matrix.

As shown in Table 1, a case falls into the Green Zone and is suitable for a conventional ISDS mechanism if it is not politically or socially sensitive. A dispute involving an individual act of direct expropriation might warrant this designation. In contrast, a case that is both politically and socially sensitive falls into the Red Zone. These cases should be excluded from ISDS and instead left to other venues, such as local remedies or state-to-state mechanisms under investment treaties or general international law. A dispute involving essential security and national emergency rules would fall into this category. In turn, cases that are politically sensitive but socially insensitive, such as those involving individual taxation measures or prudential measures of financial regulation, implicate the Yellow Zone. In this category, states might justifiably exert substantial control, including by relying on state-to-state dispute settlement rather than ISDS. Finally, cases that are socially but not politically sensitive, such as those involving environmental or human health measures, fall into the Blue Zone. These cases are best dealt with through enhanced social monitoring of the ISDS system, including by means of transparency requirements and amicus curiae briefs.[9]

This matrix clarifies the variable dimensions of international investment disputes. By highlighting the ways in which different types of disputes carry unique social and political implications, it helps states to weigh the comparative advantages of their reform options in light of relevant policy goals. In doing so, the matrix helps states to choose the settlement mechanisms that best serve their interests.

To be sure, the significance of substantively similar disputes might vary across states and time. For example, environmental protection might be a matter of both social and political sensitivity in some states, but only an issue of social concern in others. Similarly, matters that were not previously sensitive might become so as states develop. The methods to be chosen for settling investment disputes should vary along with these conditions. In this sense, we agree with Puig and Shaffer, and with Roberts, that diversity and pluralism should continue to be a feature of ISDS, and that flexibility is vital to the successful realization of any large-scale reform.

The Future Outlook: International Adjudicatory Mechanisms as Alternatives or Complements?

In applying the matrix and the trinity analytical framework, one cannot help but wonder at the future outcome of the current efforts toward reform. As illustrated above, our matrix analysis suggests that the mainstream solution

[8] *See* Philip Morris Asia Ltd. v. Austl., PCA Case No. 2012-12.

[9] Wenhua Shan, *Toward a Multilateral Plurilateral Framework on Investment*, The E15 Task Force on Investment Policy 8–9 (Nov. 2015).

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to international investment disputes should probably continue to be international adjudicatory mechanisms, such as ISDS (as modified), state-to-state arbitration, or straightforward international commercial arbitration (with little or no adaption), as these are likely to be used for investment disputes in each of the four zones. Local remedies, in contrast, might be more appropriate for Red Zone disputes that are so politically and socially sensitive that states will decide to keep them within their domestic jurisdiction.

From this perspective, international adjudicatory mechanisms should serve as alternatives to local remedies. Puig and Shaffer, however, contend that such mechanisms should operate only as complements, rather than as alternatives, to national courts. In their view, such an approach better serves the overarching goal of investment dispute resolution, which they say is to advance the rule of law in host states. To the extent that international adjudicatory mechanisms retain a role in this approach, it is to serve as a check against defective decisions by municipal courts.

Puig and Shaffer's proposal may be sensible in the long-term, once the rule of law has progressed beyond its current state. But it is unclear whether it fits the current global reality. As Puig and Shaffer admit:

> In the end, the effectiveness of complementarity mechanisms depends on the existence of some level of judicial independence and impartiality in the domestic jurisdiction, combined with some level of trust across the domestic/international divide. Where these conditions are present, complementarity mechanisms can be both fair and effective. Moreover, they can work dynamically to enhance rule-of-law protections over time. Where these conditions are lacking, then complementarity mechanisms could be dysfunctional or at least increase the cost of dispute settlement.[10]

The fundamental question, then, is whether such conditions exist in the world in general and between investment treaty partners in particular.

The World Justice Project's Rule of Law Index (RLI) helps to provide an answer. Rating states on a scale from one to zero to indicate the degree of their adherence to the rule of law, the latest RLI reports that only twenty-two states out of 113 score above 0.7 and only thirty-eight states score above 0.6.[11] All other states score at 0.6 or less, which means that they exhibit "weaker adherence to the rule of law."[12] The World Justice Project's survey of civil justice systems reports a similar result, with only thirty-eight states scoring at 0.6 or above.[13] This suggests that the vast majority of states—roughly two-thirds in total—are still struggling to achieve the rule of law and quality civil justice.

To make matters worse, most investment treaties do not exist between states that exhibit a strong commitment to the rule of law. Indeed, only 249 investment treaties have been signed between the thirty-eight states with a score of 0.6 or higher in civil justice. This amounts to a mere 12.89 percent of the 1931 investment treaties that have been signed among the 113 states.[14] In other words, nearly 88 percent of investment treaties count as a party a state with an underdeveloped civil justice system. In this context, it is difficult to argue for a change of the investment dispute settlement regime toward a system that privileges municipal courts. Such an approach would place many disputes in fora that are poorly equipped to provide an effective and just resolution.

It is true that the losing party in municipal court could resort to international adjudicatory mechanisms under Puig and Shaffer's proposal. But the underdeveloped state of many civil justice systems suggests that this approach

[10] Puig & Shaffer, *supra* note 1, at 407.

[11] World Justice Project, Rule of Law Index 2017–2018, at 20 (June 2018).

[12] *Id.* at 22–23.

[13] *Id.* at 44.

[14] *See* UN Conference on Trade & Dev., Investment Policy Hub: International Investment Agreements Navigator (providing statistics).

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would generate many attempts to use international mechanisms to correct municipal decisions. Such a result would run directly against the efficiency goal that Puig and Shaffer identify. It would also raise acute sovereignty concerns.

A more realistic approach would be to allow foreign investors to resort to international adjudicatory mechanisms as an alternative to municipal courts. Such mechanisms might have to be reformed, balanced, and upgraded depending on the attending circumstances. But in general, allowing investors to resort to international mechanisms would empower them to choose the forum that is best suited to their dispute. It would also limit the inefficiency of complementarity and generate fewer cases in which international actors must review disputes that municipal courts have already decided.

Conclusion

The articles by Puig and Shaffer, and Roberts, make significant contributions to ongoing discussions about ISDS reform. They provide sound analyses from the perspective of methods (the varied institutional choices for investment dispute settlement) and subjects (the different categories of states involved), respectively. But the MAF provides a necessary supplement by emphasizing the importance of the objects of dispute settlement—i.e., the disputes themselves. By combining analyses of methods, subjects, and objects into a trinity, states can gain a better sense for the types of reform that might best suit their interests. That said, not all reforms are equal. While diversity and pluralism are likely to continue as key features of ISDS reform, it would be better for states to view international adjudicatory mechanisms as alternatives, rather than as complements, to municipal courts in the context of investment disputes.

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