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Possible reform of investor-State dispute settlement (ISDS)

Submission from the Government of Colombia

Note by the Secretariat

The present note reproduces a submission received on 13 June 2019 from the Government of Colombia in preparation for the thirty-eighth session of Working Group III. The submission is reproduced as an annex to this note in the form in which it was received.

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Annex

[English and Spanish]

Submission by Colombia on potential procedural solutions of reform[1]

A. Introduction

1. According to the Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-seventh session,[2] the Working Group decided, among other things, that submissions to the Secretariat should be made by 15 July 2019 on what other solutions to develop, and when such solutions might be addressed in terms of the project schedule.

2. Taking into account such agreement, Colombia, as a member State of UNCITRAL, wishes to present what it considers could be a plausible procedural approach to follow, in order to move forward and to implement with flexibility and progressivity the measures that address the concerns already identified by the Working Group. In the present proposal, Colombia does not present a solution to each of the concerns raised by member States, but rather a methodology of how to address them in an effective manner. As such, the substantive provisions referenced in the proposal are drawn from document A/CN.9/WG.III/WP.149[3] and from the other issues discussed at the thirty-seventh session.

3. The Working Group has already agreed that the development of reforms by UNCITRAL was desirable to address: (i) concerns regarding lack of consistency, coherence, predictability and correctness of arbitral decisions by ISDS tribunals; (ii) concerns pertaining to arbitrators and decision makers; and (iii) concerns pertaining to cost and duration of ISDS cases.[4] Moreover, the outcome of discussions at the thirty-seventh session showed that other concerns not covered by the three broad categories deserved attention and needed to be considered.[5] The procedure to attain such goals, however, does not appear to be a simple one. It is time to envisage potential procedural approaches for implementing the measures that address the concerns already identified.

B. The proposal

4. From Colombia's perspective, it would be useful to take into account other experiences of international organizations, such as the Organization for Economic

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[1] This proposal is without prejudice to the position of Colombia on the outcome of the ongoing discussions of Working Group III regarding ISDS reform solutions.

[2] Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-seventh session (New York, 1–5 April 2019). Document A/CN.9/970. Distr. General.: 9 April 2019. Original: English. https://uncitral.un.org/sites/uncitral.un.org/files/acn9_970_as_sub_1.pdf.

[3] Possible reform of investor-State dispute settlement (ISDS). Note by the Secretariat. Document A/CN.9/WG.III/WP.149. Distr.: Limited. 5 September 2018. Original: English. United Nations Commission on International Trade Law. Working Group III (Investor-State Dispute Settlement Reform). Thirty-sixth session. Vienna, 29 October–2 November 2018. https://undocs.org/en/A/CN.9/WG.III/WP.149.

[4] Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-sixth session (Vienna, 29 October–2 November 2018). Document A/CN.9/964. Distr.: General. 6 November 2018. Original: English. https://undocs.org/en/A/CN.9/964.

[5] Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-seventh session (New York, 1–5 April 2019). Document A/CN.9/970. Distr.: General. 9 April 2019. Original: English. https://uncitral.un.org/sites/uncitral.un.org/files/acn9_970_as_sub_1.pdf.

Cooperation and Development (OECD).[6] A potential approach would be to replicate the model followed during the negotiation of the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting – MLI*,[7] (hereinafter "The Model").

5. Colombia considers that the Model offers an enormous advantage as it has a large degree of flexibility, such that UNCITRAL member States can accommodate themselves to it according to their interests and concerns, as will be further explained. In this regard, the core purpose of this proposal is to contribute in a constructive and active manner to the work to be done by the Working Group. Furthermore, Colombia wants to take advantage of this submission to stress its willingness to achieve a substantive reform that responds to the interests of Governments and also makes it possible to quickly tackle some gaps and deficiencies faced by the ISDS system.

6. To this end, Colombia takes note of the proposals submitted by other member States. In particular, Colombia would like to refer to the submission by Chile, Israel and Japan,[8] highlighting the valuable contribution of the idea of a "menu" of solutions. Also, Colombia would like to refer to the observations presented by Indonesia[9] and the concerns expressed regarding ISDS and the need to tackle them in the reform process, those concerns being fully shared by Colombia. Similarly, Colombia welcomes the willingness shown by the European Union and its Member States through their submission early this year[10] regarding the possibility of considering an open architecture in connection with the idea of a permanent structure, especially as some countries may wish to retain degrees of flexibility.

7. The structure of this proposal is, then, as follows: first, a brief introduction to the OECD Model used in the taxation treaties domain; second, an explanation of how it would work, detailing the functions and operation of the Model; third, an explanation of how this model could be a point of reference to follow in ISDS discussions; fourth, some thoughts on the benefits of replicating this model within our current UNCITRAL discussions; and finally, a proposed outline/menu of the movable parts that could comprise an UNCITRAL ISDS reform model.

8. Colombia wishes to extend a kind invitation to all Governments to take a close look at this potential procedural idea, as a way in which each one could find its own spaces, its quick fixes or systemic reforms, with different speeds and contents, with potential future arrangements and, above all, with a unique multilateral instrument common to all countries.

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[6] Proposal for Work Plan of Working Group III Submitted by the Delegations of Chile, Israel and Japan. Document A/CN.9/WG.III/WP.163. Distr.: Limited. 15 March 2019. Original: English. United Nations Commission on International Trade Law. Working Group III (Investor-State Dispute Settlement Reform). Thirty-seventh session. New York, 1–5 April 2019. https://undocs.org/en/A/CN.9/WG.III/WP.163. p. 1 (iv).

[7] Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("Multilateral Instrument" or "MLI"). The Organization for Economic Cooperation and Development (OECD). https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm.

[8] Proposal for Work Plan of Working Group III Submitted by the Delegations of Chile, Israel and Japan. Document A/CN.9/WG.III/WP.163. Distr.: Limited. 15 March 2019. Original: English. United Nations Commission on International Trade Law. Working Group III (Investor-State Dispute Settlement Reform). Thirty-seventh session. New York, 1–5 April 2019. https://undocs.org/en/A/CN.9/WG.III/WP.163.

[9] Possible reform of Investor-State dispute settlement (ISDS). Comments by the Government of Indonesia. Document A/CN.9/WG.III/WP.156. Distr.: Limited. 9 November 2018. Original: English. United Nations Commission on International Trade Law. Working Group III (Investor-State Dispute Settlement Reform). Thirty-seventh session. New York, 1–5 April 2019. https://undocs.org/en/A/CN.9/WG.III/WP.156.

[10] Establishing a standing mechanism for the settlement of international investment disputes. Submission from the European Union and its Member States. Document A/CN.9/WG.III/WP.159/Add.1. Distr.: Limited. 24 January 2019. Original: English, French and Spanish. https://undocs.org/en/A/CN.9/WG.III/WP.159/Add.1.

C. The “MLI Model”

(a) A brief introduction

9. In order to tackle Base Erosion and Profit Shifting (BEPS),[11] the OECD developed a BEPS Action Plan, endorsed by the G20 in 2013, identifying 15 actions to address BEPS in a comprehensive manner.

10. Later, in 2015, the OECD adopted the BEPS Package, which includes measures under four Actions that involve changes to the existing network of bilateral tax treaties: (i) Action 2 on Hybrid Mismatches; (ii) Action 6 on the Prevention of Treaty Abuse; (iii) Action 7 on Avoidance of Permanent Establishment Status; and (iv) Action 14 on Improving Dispute Resolution.

11. Action 15 of the BEPS Action Plan provided for an analysis of the possible development of a multilateral instrument to implement tax treaty related BEPS measures “to enable jurisdictions that wish to do so to implement measures developed in the course of the work on BEPS and amend bilateral tax treaties”.[12] Such analysis led to the conclusion that a multilateral instrument using an approach that enabled countries to swiftly modify their bilateral tax treaties to implement measures developed in the course of the work on BEPS was desirable and feasible, and that negotiations for such an instrument should be convened.

12. For this task, an ad hoc Group was formed, open to all interested countries (99 countries participated).[13] As mentioned before, the BEPS Package had already identified the measures under Actions 2, 6, 7 and 14 that would require changes to the existing network of bilateral tax treaties. Therefore, the negotiation in the ad hoc Group, which started in May 2015, was focused on how the Convention would need to modify the provisions of bilateral or regional tax treaties in order to implement those measures.

13. The negotiations of the ad hoc Group concluded in November 2016 and the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (The Multilateral Instrument or MLI) was signed by over 70 jurisdictions in June 2017 and entered into force in July 2018.[14]

(b) How does the MLI work?

14. As noted above, the MLI is aimed at modifying tax treaties between two or more Parties to the MLI, when those tax treaties have been listed by both Contracting Jurisdictions as an agreement they wish to be covered by the MLI.[15] In this sense, it does not function in the same way as an amending protocol to a single existing treaty,

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[11] Tax planning strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations where there is little or no economic activity, resulting in little or no overall corporate tax being paid.

[12] Note by the OECD Directorate of Legal Affairs. Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (“Multilateral Instrument” or “MLI”). The Organization for Economic Cooperation and Development (OECD). https://www.oecd.org/tax/treaties/legal-note-on-the-functioning-of-the-MLI-under-public-international-law.pdf.

[13] Explanatory Statement to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting. The Organization for Economic Cooperation and Development (OECD). https://www.oecd.org/tax/treaties/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf.

[14] Information Brochure. Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting. The Organization for Economic Cooperation and Development (OECD). https://www.oecd.org/tax/treaties/multilateral-instrument-BEPS-tax-treaty-information-brochure.pdf.

[15] Note by the OECD Directorate of Legal Affairs. Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (“Multilateral Instrument” or “MLI”). The Organization for Economic Cooperation and Development (OECD). https://www.oecd.org/tax/treaties/legal-note-on-the-functioning-of-the-MLI-under-public-international-law.pdf.

which would directly amend the text of the tax treaties covered by the MLI. Instead, it will be applied alongside existing tax treaties, modifying their application in order to implement the BEPS measures.[16]

15. The MLI Convention is designed following the common structure of international instruments, consisting of a set of articles establishing the scope of the agreement, its definitions, the substantive provisions (the BEPS measures) and finally the institutional provisions.

16. The novelty of the MLI is the flexibility it grants to Parties to comply with the substantive provisions. First of all, it allows each Party to specify the tax treaties to which the Convention will apply, allowing ample scope and flexibility for countries to decide, progressively, according to their own interests. When two parties specify a mutual treaty, a "match" occurs, and a new layer of rules then applies to that treaty. Second, the MLI provides different alternatives to satisfy those provisions that represent minimum standards, without giving a preference to a particular way of meeting the minimum standard. Third, in case a substantive provision does not reflect a minimum standard, a Party is given the flexibility to opt out of that provision. Fourth, a Party has the possibility of opting out of provisions or parts of provisions with respect to tax treaties covered by the MLI that contain existing provisions with specific characteristics. Fifth, the Convention incorporates a number of alternatives or optional provisions which each Party can choose to apply.[17]

17. It is of relevance to note that under the provisions of the MLI, each jurisdiction is required to provide a list of notifications at the time of signature. The notifications refer, for instance, to the list of tax treaties to which the MLI will apply, and the option chosen for the fulfilment of an obligation under a specific article.

18. As a practical example, "Article 4 - Dual Resident Entities" of the Convention establishes that, where by reason of the provisions of a bilateral tax treaty a person is a resident of more than one Contracting Jurisdiction, the competent authorities of the Contracting Jurisdictions shall endeavour to determine by mutual agreement the Contracting Jurisdiction of which such person shall be deemed to be a resident for the purposes of the bilateral tax treaty concerned. As Article 4 does not reflect a minimum standard, a Party can opt in or opt out of it entirely or partially. For instance, Luxembourg and the Czech Republic have both notified their bilateral tax treaty (a match occurred), so the MLI will apply in general to that treaty. However, in this particular case of Article 4, both Parties have also notified that they will opt out of Article 4 of the Convention, meaning that under their bilateral tax treaty, Article 4 of the Convention will not apply.

D. The MLI as a model to be considered by Working Group III

19. Regarding the work ahead in phase three of reform by Working Group III, Colombia wishes to reiterate its gratitude to Chile, Israel and Japan for their valuable proposal submitted in March, in particular, the idea of contemplating sufficient flexibility to develop a menu of possible solutions, which may vary in form, and that member States can choose to adopt, based on their specific needs and interests. Colombia considers that one way to reflect a concrete menu of possible solutions as proposed may be to explore the possibility of replicating the model followed by the OECD in the negotiation of the MLI.

20. In the negotiation of the MLI, elements quite similar to the ones presented by Chile, Israel and Japan in their submission were taken into account. The negotiation focused mainly on modifying the application of bilateral tax treaties to eliminate

[16] Explanatory Statement to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting. The Organization for Economic Cooperation and Development (OECD). https://www.oecd.org/tax/treaties/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf.

[17] Ibid.

double taxation based on the solutions and options agreed in the MLI, giving States a broad framework of flexibility to make adjustments, as necessary, to their current international obligations and agreements according to their interests.

21. Thus, the MLI allows States to specify the tax treaties to which the Convention would apply, and provides the extra flexibility of opting out of provisions with respect to all tax treaties covered by the MLI that do not reflect a minimum standard. Parties are also allowed to choose to apply optional or alternative provisions with specific characteristics.

22. The multilateral negotiation established a set of "minimum standards" for a State to accede to the Convention. In other words, the States defined some obligations that needed to be complied with by all States in order to join the multilateral agreement, but it provided options and flexibility for the rest of the provisions. The "minimum standard", in the case of UNCITRAL negotiations, could be fulfilled by the issues where there is a high degree of consensus among States in Working Group III (what some have called "quick fixes").

23. Furthermore, this alternative may be a solution to incorporate, in a single step, the developments of international investment law in the vast network of International Investment Agreements (IIAs), as was also the case in the vast network of tax treaties. This model also has the advantage of flexibility, transparency and clarity, besides its multilateral nature. Procedurally, what is needed is to establish the "menu" of measures, then specify some "minimums" for every participant, and then the ways in which notifications of IIAs covered by the convention for every block would be awarded. Potentially, UNCITRAL's solution could be simpler than the MLI. It is worth noting that the MLI model shares some similarities with the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration, in the sense that both instruments are based on opt-in solutions. A crucial difference is that the MLI does not need to be opted-into integrally, but rather can be done provision by provision, and it allows for progressivity as more and more treaties are notified under each relevant provision.

E. Benefits of using the MLI as a model

24. The ongoing ISDS reform discussions that are taking place at Working Group III share common features with the MLI experience. Indeed, the network of investment and tax treaties is quite vast: according to estimates, there are 2,932 IIAs[18] and around 3,000 tax treaties.[19] The fragmentation of the two systems, due to the vast number of treaties, has given rise to, or amplified, several concerns. In the investment system, concerns include the lack of consistency and coherence of the ISDS system, the independence and impartiality of arbitrators, the costs and duration of ISDS cases, as well as other issues. Similarly, in the tax treaties system the concerns centre on how to tackle abuses and lack of consistency: countries wish to curb tax avoidance strategies that use tax treaties to artificially shift profits to low or no-tax locations. Thus, in both forums, countries have reached the conclusion that a reform was needed, based on the concerns arising from the real functioning of investment and tax treaties. In both cases, however, this consensus was not easy, given the problems of finding shared options on how to address it.

25. These facts point up the need for a multilateral solution that ensures that treaties are used according to their purpose and object, thus avoiding treaty abuse and treaty shopping. Replicating the MLI model can lead to a swift multilateral solution, representing gains in terms of time and efficiency as countries would not need to

[18] United Nations Conference on Trade and Development (UNCTAD). Investment Policy Hub. International Investment Agreements Navigator. https://investmentpolicyhubold.unctad.org/IIA.

[19] Brochure: OECD work on taxation. The Organization for Economic Cooperation and Development (OECD). http://www.oecd.org/tax/exchange-of-tax-information/centre-for-tax-policy-and-administration-brochure.pdf.

embark on bilateral renegotiations of their IIAs in order to implement the solutions envisaged by Working Group III.

26. Furthermore, the advantage of following the MLI model is the flexibility it represents. Certainly, given the broad range of countries and jurisdictions that are involved in developing ISDS reform, the MLI model would be flexible enough to accommodate the positions of different countries and jurisdictions while remaining consistent with the purpose of the reform, while establishing some "minimums" or "pillars" to be agreed by the States.

F. A preliminary outline of an UNCITRAL ISDS reform model

27. In order to replicate the MLI model, the Working Group would need to define:

- Which issues would be part of the ISDS reform? Headway has been made in this task in the form of the three broad categories of concerns identified by the Working Group plus the other issues discussed in the framework of the thirty-seventh session and in submissions by member States.
- Which issues would constitute minimum standards? This is an exercise that would be part of the negotiation process itself which should start at the upcoming sessions.
- How would the process of opting into (or opting out of) non-minimum standards work? One possibility might be the existence of a match in notification for each block of measures; or the possibility of opting out of particular blocks of measures after a general match has occurred; or a set of options inside each block of measures for those that have had a match.

28. Taking into account that the Working Group has already identified three broad categories of concerns as well as other possible issues, a preliminary outline of a model convention could simply contain an illustrative list of substantive provisions addressing such concerns. It will be up to the Working Group to decide, during the course of the negotiations, which of those substantive provisions would constitute minimum standards and which would not. The other parts of the Convention (i.e., scope, institutional measures, etc.) would replicate the traditional articles included in most international agreements.

29. Colombia would like to propose for discussion an initial outline for the proposed multilateral treaty, with countries indicating (with an asterisk) their preferences as to which "blocks" should be considered as part of minimum standards. In the current proposal, Colombia has indicated which blocks should represent minimum standards. Countries wishing to sponsor specific drafting suggestions for solutions are encouraged to do so. This initial proposal on substantive provisions draws on document A/CN.9/WG.III/WP.149 [20] and the other issues discussed at the thirty-seventh session. As mentioned above, the definition of what issues would constitute minimum standards is an exercise that would be part of the negotiation process itself.

[20] Possible reform of investor-State dispute settlement (ISDS). Note by the Secretariat. Document A/CN.9/WG.III/WP.149. Distr.: Limited. 5 September 2018. Original: English. United Nations Commission on International Trade Law. Working Group III (Investor-State Dispute Settlement Reform). Thirty-sixth session. Vienna, 29 October–2 November 2018. https://undocs.org/en/A/CN.9/WG.III/WP.149.

A preliminary outline of an UNCITRAL ISDS reform model for implementing reforms:

MULTILATERAL CONVENTION TO IMPLEMENT INVESTMENT TREATY RELATED MEASURES TO ENSURE THE ISDS SYSTEMS OF THESE TREATIES ARE USED IN ACCORDANCE WITH THEIR INTENDED OBJECT AND PURPOSE

Preamble

PART I COMMON SCOPE AND INTERPRETATION OF TERMS	
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PART II CONSISTENCY, COHERENCE, PREDICTABILITY AND CORRECTNESS OF ARBITRAL DECISIONS BY ISDS TRIBUNALS	
Article 3	Interpretation of Substantive Standards*
Article 4	Mechanisms to Address Inconsistency and Incorrectness of Decisions*
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PART III ARBITRATORS AND DECISION MAKERS	
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Article 7	Challenge Mechanisms of Arbitrators*
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Article 14	Third-party Funding*
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Article 23	Signature, Ratification, Acceptance, Approval, Accession
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Article 27	Interpretation and Implementation
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Article 29	Entry into Force
Article 30	Withdrawal/Denunciation of this Convention
Article 31	Relation with Protocols
Article 32	Depositary

30. It is worth noting that the negotiation, implementation and administration of a model like the MLI in the framework of UNCITRAL, for all its merits, may entail in any case significant human and financial resources for the organization and validation of matches, options and reservations, thus probably requiring a permanent body or secretariat in charge of such duties. From Colombia's point of view, UNCITRAL or the International Centre for Settlement of Investment Disputes (ICSID) could be potential and appropriate candidates to perform such a task. Colombia is of course willing to discuss other alternatives to create an organ of administration of and compliance with the convention.

G. Conclusions

31. Several facts, among them the growing number of Investor-State Disputes registered during the last 15 years, have exacerbated criticism of the legitimacy of the investment protection system as well as the usefulness of the IIAs for many States. The crisis faced today by the investment protection regime requires joint, flexible and feasible solutions.

32. Colombia believes that following the MLI model can lead to a rapid and plausible multilateral outcome to implement the solutions envisaged by Working Group III thanks to the high degree of flexibility provided. This model could support the progress of discussions by presenting a methodology to address each issue.

33. Here, Colombia does not present a solution to each of the concerns raised by member States, but rather a methodology of how to address each of them in an effective manner in order to move forward. The substantive issues should emerge from the upcoming discussions by UNCITRAL member States, but this procedure could provide the space for constructive engagement.