DECIPHERING THE DYSTROPHIC RIDDLE OF TRANS-PACIFIC PARTNERSHIP AGREEMENT'S ISDS: IS IT REALLY WORTH JOINING, INDONESIA?[*]

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Abstract

*Indonesia's discomfort of being overly exposed to international claims lodged by foreign investors is prominent – up to the point wherein it intended to terminate or let lapse all of its Bilateral Investment Treaties ("**BIT**") in 2014. In the same year, Indonesia declared its intention to join the Trans-Pacific Partnership Agreement ("**TPPA**"), a newly emerging and potentially the largest free-trade agreement worldwide. In light of the foregoing, this Article will focus on TPPA's investment chapter, particularly the Investor-State Dispute Settlement ("**ISDS**") provision, as a ground to justify Indonesia's intention to join the TPPA considering Indonesia's well-known discomfort over ISDS provisions currently exist in its BITs. On its façade, TPPA's investment chapter purports to heal the past wounds inflicted by ISDS systems upon States by containing safeguards to cushion host-States' common fears of being attacked by foreign investors' claims. This either tilt heads in disapproval or spark an interest for countries to join. The debatable credibility of TPPA's ISDS provision gave rise to this Article's analysis on whether such provision would really console some of the concerns of host-States, specifically Indonesia, in relation to the ISDS mechanism currently in force in their investment treaties.*

Intisari

Indonesia terkenal atas ketidaknyamanannya untuk terlibat dalam klaim internasional yang diajukan oleh investor asing—sampai-sampai berniat untuk mengakhiri semua Perjanjian Investment Bilateral (Bilateral Investment Treaties/"BIT") pada tahun 2014. Di tahun yang sama, Indonesia mengutarakan niatnya untuk bergabung dalam Trans-Pacific Partnership Agreement ("TPPA"), sebuah perjanjian perdagangan bebas baru yang berpotensi menjadi perjanjian perdagangan bebas terbesar di dunia. Artikel ini akan fokus kepada bagian investasi dari TPPA, khususnya pada pasal penyelesaian sengketa antara Investor dan Negara (Investor-State Dispute Settlement/"ISDS"), sebagai dasar pembenaran niat Indonesia untuk bergabung dengan TPPA, dengan mempertimbangkan ketidaknyamanan Indonesia atas pasal-pasal ISDS yang ada di BIT saat ini. Pasal-pasal investasi TPPA dimaksudkan untuk menenangkan Negara dengan memberi perlindungan kepada Negara tuan rumah dari serangan klaim investor Asing, walaupun mengundang celaan dari beberaoa pihak. Kredibilitas yang belum pasti dari pasal-pasal ISDS TPPA memunculkan analisis dari Artikel ini, bahwa apakah ketentuan tersebut akan menyembuhkan ketakutan Negara, Indonesia khususnya, dalam hubungannya dengan mekanisme ISDS yang saat ini sedang berlaku di perjanjian investasinya

Keywords: Trans-Pacific Partnership Agreement, Investor-State dispute settlement, foreign direct investment, Indonesia

Kata Kunci: Trans-Pacific Partnership Agreement, penyelesaian sengketa Investor-Negara, investasi asing langsung, Indonesia.

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A. Introduction

Should it finally be ratified, the Trans-Pacific Partnership ("**TPP**") will be the largest free trade area in the world. The agreement itself, TPPA, was released in late November 2015, and compressively covers rules ranging from, Technical Barriers, Telecommunications, Rules of Origin, Intellectual Property, Investment Protection, and many more.

TPPA was negotiated, and subsequently concluded, by twelve Pacific Rim countries: Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States and Vietnam (Tung, 2015), which represent almost 40% of the global trade. Since then, more countries are willing to join this partnership.

Indonesia is one of those countries. In 2015, President Joko Widodo told Barrack Obama, the United States President, that Indonesia is interested in signing the TPPA (Ginanjar (BBC Indonesia), 2015). Joining TPP will definitely bring considerable changes to Indonesia considering the comprehensive and extensive regulations covered by the agreement, but the balancing weight of whether or not Indonesia should join must eventually be discussed more than in one writing.

This Article, meanwhile, draws attention to Indonesia's decision to terminate its BIT with Netherlands in 2014, and its concurrent declaration that it will not renew all of its existing BITs (Van den Pas & Damanik, 2014; Beckmann et al, 2014). Out of all the varying reasoning, the turning point was definitely Indonesia's recent legal exposure against foreign investors' claim. The *Churchill* case served as one example, in which Indonesia is currently facing the prospect of losing out 1 billion USD claims against a multinational British Company *Churchill* before ICSID Tribunal, as it lost in the jurisdiction phase, whereas the merits remain pending (*Churchill Mining v. Indonesia*; *Planet Mining v. Indonesia*).

Following the aforementioned events, Indonesia's then-President, Susilo Bambang Yudhoyono, emphasized that he does not want multinational companies to put pressure on developing countries like Indonesia (American Chamber of Commerce in Indonesia, 2014). Even though talks and suggestions have been circulating regarding Indonesia's plan to only renegotiate its current BITs, none has been finalized yet (Crocket, 2015; Oegroseno, 2014; Amianti, 2015). The message though was clear: Indonesia was not comfortable with its excessive legal exposure against claims from foreign investors.

Now, presuming that Indonesia would eventually let lapse or at least renegotiate all of its BITs, Indonesia would definitely try to limit the legal exposure to avoid investor's claims over investments that Indonesia never intended to provide BIT protections to. If Indonesia were to be successful in doing so, it would be interesting to examine whether TPPA would provide Indonesia with the kind of provisions it desires presently – or instead, whether TPPA would drag Indonesia back to square one with all of its concerns regarding its excessive legal exposure.

In this line, it is crucial first to discuss the provision that allows multinational companies to bring international claims against State directly before international tribunals, which is the ISDS provision.

B. ISDS and Host-State's Concerns

ISDS is a system that enables investors to directly sue a host-State for any violations of investment-related protections. Generally, investors prefer to sue host-States through international arbitration. In most BITs, access to international arbitrations are provided for investors, either directly or following satisfaction of certain conditions such as cooling-off periods or recourse to national courts for certain period of time.

Admittedly, ISDS, and through its extension, international arbitration, has become one of the most frequently invoked provisions by foreign investors over the past two decades. It is not telling that investors tend to rely on this provision to bring their disputes before international arbitration, as investors are often reluctant to go to host-States courts (Miller & Hicks, 2015).

This was generally accepted in cases wherein host-States were eager to promote their investments, especially when these States were in the stage of developing, such as Indonesia. This is probably why at least in 60 out of 64 BITs concluded by Indonesia with various States, Indonesia has provided its standing consent to arbitrate against any qualified investors wishing to submit a dispute in arbitration (Churchill, ¶ 204).

Access to arbitration, as provided by most of ISDS mechanism, is not exactly a bad thing for host-States. However, it does become a concern when investors are allowed to abuse this provision by bringing frivolous claims, or when tribunals misinterpreted the scope of its jurisdiction due to the insufficient definitions of various terms of the treaties.

For example, the unclear definition of the term 'investment' in Indonesia-UK BIT caused the tribunal in *Rivzi* to interpret the term as not being limited to foreign direct investment Company, as opposed to what Indonesia actually intended (*Rivzi v Indonesia,* ¶ 142). Although in that case *Rivzi* was eventually denied jurisdiction, the tribunal's interpretation on the term 'investment' may be relied in other cases to allow treaty protection to virtually any investment from UK, either direct or indirect.

It is cases such as this that have caused host-States to be increasingly more wary of the over-reliance on ISDS by investors (Warren, 2015). Australia's reaction towards ISDS serves as an epitome of this. Following several suits filed against Australia by tobacco-company Philip Morris over Australia's new plain-tobacco-packaging rules, Australia declared that it was against the inclusion of ISDS in TPPA (Hurst, 2015). However, upon the release of TPPA's text, Australia eventually agreed to the inclusion of ISDS, seemingly to be content with the ISDS's modifications contained in TPPA.

The questions then that this paper will subsequently try to answer is whether TPPA's ISDS would really console the various concerns host-States – especially Indonesia – over ISDS, as discussed next.

C. TPPA's ISDS

TPPA's ISDS have been regarded by some as a state-of-art, as it purports to upgrade and reformed the currently existing ISDS systems (Tung, 2015; USTR, 2015). The fact that Australia finally agreed to its inclusion may support this notion. Nonetheless, equally, there has been growing resistance towards TPPA's ISDS.

Subsequently, in order to eventually determine whether TPPA does console host-State's concerns over ISDS, a thorough analysis on the whole agreement must be done. For the purpose of this Article though, the focus will only be on the provisions that are in dire need of modifications for Indonesia, i.e. the scope of covered investment, consent to arbitration, and regulatory measures.

Further, this Article will also discuss some notable provisions that are incorporated in the TPPA that have been heralded as 'reformative', such as the provisions panels for arbitrators, appellate mechanism, and cost of arbitrations and frivolous claims (USTR, 2015.)

A. The Term Investment

As briefly mentioned, one of Indonesia's main concern over its current BITs is the term 'investment'. This term, contained in practically all investment treaties, determines which investment located in the host-State may enjoy protection from an investment treaty, and which may not. Indonesia has made it clear that its intention was only to give protections to foreign direct investment company that is allowed admission and subsequently supervised by the Indonesia Investment Supervisory Board ("**BKPM**") (Rivzi, ¶ 74, 109).

There have been at least two cases where Indonesia felt it was let down by the tribunal's overreaching interpretation on the term investment in an investment treaty. The first one is *Rivzi,* as mentioned previously.

The second one is *Al-Warraq v. Indonesia,* where Indonesia lost in jurisdiction phase, but eventually won on the merits. In *Al-Warraq,* the investment treaty relied by the investor was the Organization of the Islamic Conference Investment Treaty ("**OIC**"), which Indonesia was a party of. The OIC members had limited arbitration mechanism only for State-to-State dispute. However, due to the insufficiently clear language, the tribunal refused to follow the intention of the members and instead followed the "current trends", and thus granted the right to bring arbitration against a host-State to the investor (Al-Warraq, ¶ 76).

Now, presuming that Indonesia would eventually lapse or renegotiate all of its BITs, Indonesia is most likely to be interested to limit the meaning of the term 'investment' to only what it really intended to mean. But if Indonesia joins the TPPA, Indonesia will be on the brink of experiencing similar concern over the term 'investment' all over again.

This is because TPPA defines the term of the covered investment in the broadest style possible: "*every asset that an investment owns or controls, directly or indirectly, that has the characteristics of an investment, including such characterizes as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk*" (Article 9.1 TPPA).

Thus, it can be seen that TPPA intended to cover all types of investment, either direct or directly controlled by any foreign investors from the other Member-States. Consequently, cases such as *Rivzi* or *Al-Warraq* may repeat all over again if investors were to sue Indonesia under TPPA.

B. Consent to Arbitration

Access to arbitration is definitely an important provision in any investment treaties. Notwithstanding that, it is worth to note that 'consent' is the cornerstone of arbitration and hence, an arbitration should not be commenced when both parties have not consented to such arbitration (Poudret/Besson, p. 229).

In *Churchill,* Indonesia tried to argue that the term 'shall assent to consent' does not amount to Indonesia's automatic consent to arbitrate against any investors wishing to arbitrate against Indonesia under the UK-Indonesia BIT. Despite that, the tribunal refused Indonesia's arguments and eventually allowed the investor to continue on the merits of the case (Churchill, ¶ 238-239).

Seeing that Indonesia has provided its automatic consent to arbitrate in 60 out of 64 of its BITs (61 now since *Churchill*), if Indonesia were to eventually lapse or at least negotiate all of its BITs, Indonesia is most likely to be interested to limit the scope of consent to shield them from future non-consented investor arbitrations. However, joining the TPPA would hinder such interest, since Article 9.19 TPPA stipulates "*each Party consents to the submission of a claim to arbitration under this Section in accordance with this agreement*", which simply enables investors to bring disputes to arbitration against Indonesia any time they desire. In other words, Indonesia will be treated as if they have automatically consented to arbitrate.

The only limitation to arbitration provided under TPPA is only the 6-months cooling-off period where investors are obliged to conduct amicable consultations first. But bearing in mind that arbitral tribunals in the past have regarded a cooling-off period provision as mere procedural nicety rather than condition to arbitration, such limitation is as good as moot (Born/Scekik, p. 239).

Consequently, signing the TPPA is equivalent to Indonesia's automatic consent to arbitrate against investors from at least its 12 current members – which seems to foreshadow a distressful experience, especially reminiscing back on the *Churchill* case.

C. Regulatory Measures

In international investment law, one of the most heated debate is the distinction between what constitutes as expropriation and what is considered as regulatory measures. While the former entails compensatory obligation, the latter does not (Saluka, ¶ 262). However, the distinction is often too vague and investors tend to abuse any measures imposed by a host-State to be amounting expropriation if such measure were to harm their investments in any way.

For example, related to Indonesia, in both *Rivzi* and *Al-Warraq,* the investors claimed expropriation of their investment upon the decrease of the relative percentage of the whole of the capital of their shares in Bank Century, although the percentage decrease actually did not affect their overall ownership of their shares. The decrease was actually caused by Indonesia government's decision to help Bank Century by injecting a great amount of capital to save the very same bank (Rivzi, ¶ 38; Al-Warraq, ¶ 44).

Although both investors did not prevail in their respective expropriation claims, it is wise for Indonesia in the future to make sure that it is capable of adopting a measure for the good of the State without running the risk of being sued by foreign investors who are dissatisfied with such measure.

At a glimpse, TPPA ensures that host-States are guaranteed with protection to adopt a regulatory measure without being subjected to investors' expropriation claims. Article 9.15 TPPA provides: *"Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining or enforcing any measure <u>otherwise consistent with this Chapter</u> that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental, health or other regulatory objectives."*

Arguably, this provision is the bait that successfully lured Australia to accept ISDS inclusion in TPPA. The Australian trade minister even praised the provision by describing it as a safeguard that will protect new environmental and health policy and regulations from lawsuits by foreign investors (Ludlam, 2016).

That is not entirely true. The wording '*otherwise consistent with this Chapter*' is a disguised loophole for investors to trample the sovereignty of states. In other words, *any* measure adopted by a host-State, whether it be on health or environmental regulatory grounds, must be consistent with the TPPA. In spite of the fact that tribunals have no authority to force a government to change the laws put into question by an investor, governments often step back from imposing a certain measure to avoid having to pay compensatory damages (Kelsey & Wallach, 2012).

Therefore, with so much room for an overreaching interpretation, investors are naturally inclined to argue that any regulatory measure adopted by host-States that may have harmed their investments in any way amounts as amounting to expropriation. It appears that a State's right to perform its regulatory measures is viewed as subordinate to the other provisions of the investment chapter (Tung, 2015). With that in mind, the position of foreign investors are elevated to an equal standing with each TPPA's signatory members – potentially including Indonesia.

D. Independence and Impartiality of Arbitrators

Arbitral tribunals consist of private individuals who are entrusted with the power to review government actions and award compensation damages – which is why independence and impartiality of arbitrators are crucial. In practice though, studies have revealed that over 50% of ISDS arbitrators have also acted as counsel for investors in other ISDS cases (Gaukrodger & Gordon, 2012) and that most agreements lack substantive conflict of interest disclosure requirements (Knox & Markell, 2012).

The design of ISDS tribunals allows lawyers to 'change hats' or rotate between dual roles in a manner that would be unethical for judges (Evatt, Thomas, Wilson et. al., 2012). Consequently, the candidate pool is sometimes seen as biased (UNCTAD, 2013) and awards are granted through unhealthy compromises (Gaukrodger & Gordon, 2012). Obviously, this fear is not entirely justified as there are too still arbitrators that are both independence and impartial. Nevertheless, there is an existing concern to combat this issue amongst host-States.

To a certain extent, the same holds true for Indonesia. For example, Indonesia lost twice in jurisdiction phase in two different cases: *Al-Warraq* and *Churchill*. Both cases involve, at least according to Indonesia, a misinterpretation of the scope of jurisdiction of the tribunals in a way they applied broad interpretation of the term 'investment' and 'consent' respectively, thus favoring the investor to proceed to the merits of the case (Al-Warraq, ¶ 76; Churchill, ¶ 238). Although surely the tribunals had justifications on their respective finding, it is interesting to note that the two cases shared one same arbitrator.

To facilitate such concern, TPPA intends to create a code of conduct for arbitrators in ISDS. As of now, such code is not yet established, yet if there was to be any indication, it will not facilitate the said concern at all. This indication can be found in Article 28.10(d), where TPPA has established a code of conduct for the general Dispute Settlement's panelists. Under this article, all panelists must comply with the code of conduct in the Rules of Procedure enshrined in Art. 28.13.

Strangely though, the so-called code of conduct is not enforced by an independent entity outside the dispute. Rather, it would be established by TPP's Commission, composed of government representatives of each party at the level of ministers or senior officials (Art. 27.1 TPP). On top of that, there are no ethical canons or principles stipulated for guidance or to explain how these arbitrators should behave or act.

Should these indications are applied to ISDS as well, then alas, what is essential to prevent the legal uncertainty, conflict of interests or any abuse of discretion, is actually missing in TPPA.

E. Appellate Mechanism

Due to its awards that are final with no recourse to appeal, arbitration is reputable for conducting fast proceedings. Despite that, there have been inconsistent legal findings for the same cases based on the same facts by different arbitral tribunals.

This is exactly what happened when four American energy companies, CMS Transmission Co., LG&E Energy Corp., Enron Corp., and Sempra Energy International filed the same claim separately against Argentina under the 1991 U.S-Argentina BIT (Alvarez & Khamsi, 2009). Such divergent decisions create difficulty for States to enforce adopt measures that will not breach its international obligations to foreign investors.

Even though there have not been exactly such similar inconsistency in arbitral tribunal's findings that are related to Indonesia, the fact that Indonesia is infamously known for its reputation for being reluctant to enforce foreign arbitral award since *Karahabodas* case may shine some light to the concerning nature of the finality of foreign arbitral awards in Indonesia (Al-Gozaly, p. 130)

That being said, creating an appellate body for investment arbitration might be a possible solution to bring consistency in decisions that would satisfy both host-States and investors alike. A final ruling by an appellate body would have been able to bring consistency to the result, thereby treating all similarly situated investors with uniformity, providing a clear guidance for host-State with respect to its economic measures and contribute to the development of investment treaty law (Tung, 2015).

Possibly, it was in this line that TPPA's ISDS makes room for the establishment of an appellate body (Art. 9.22(10) TPP). Even so, this possibility was not first made by TPP. In fact, in the 2012 US Model BIT, the same provision can be found in Article 28 where the US was open to the idea of future appellate mechanism for investment arbitration. Thus, it was somehow regrettable that TPP member states did not actually develop the appellate mechanism that has been contemplated since back in 2012.

F. Cost of Arbitration Proceeding and Frivolous Claims

Host-States are repelled to borne the costs of ISDS proceedings, since there is an increasing concern regarding the economic costs and lack of accountability involved in the process (Warren, 2015). ISDS cases often result in millions of dollars in damages and litigation fees (Casale, 2015). To be more specific, the average arbitration cost of one case is US$8 million, with 80% of it being the costs of legal representation and experts, while the average arbitration fees is US$3,000 per day (Kelsey & Wallach, 2012).

Such high costs are relatively harmful to host-States, especially those that are still developing, such as Indonesia. This may be best epitomized in the still on-going *Churchill* Case that has extended beyond two years, involving 20 different procedural orders, each adding more to the arbitration's cost (*Churchill,* Procedural Orders). The recent report even suggested that Indonesia has failed to pay its fair shares of the proceedings, causing the arbitration to be in static (Newsham, 2016).

Furthermore, the high amount of cost that needs to be borne bothers host-State even more when it comes to frivolous claims. Accordingly, TPPA's ISDS intends to contain strong safeguards to prevent abusive and frivolous claims. Article 9.22(4) states that tribunal shall decide as a preliminary question about a claim that is '*manifestly without legal merit*.'

Nonetheless, other precedent investment agreements, such as NAFTA, already contains similar provisions, yet are still prone to frivolous claims. Admittedly, unlike TPPA, they do not stipulate the wording '*manifestly without legal merit*.' In spite of that, it is relatively doubtful that an addition of four words in TPPA will result in a significant improvement in prevention of frivolous claims (John & Sachs, 2015).

On the other hand, TPPA allows legal costs to be recovered by the host-State in cases of frivolous claim, but this is not to be mistaken as a relief. Long before TPPA, tribunals were already granted the power to award attorney's fees and costs against parties claiming frivolous claims (See Art. 61(2) ICSID; Art. 42 UNCITRAL; Art. 10.20(6) US-DR-CAFTA). Regardless, tribunals have been rather reluctant to exercise such powers, often instead ordering parties to bear its own costs. Subsequently, TPPA's reiteration of such power does not convince a party's ability to recover legal costs (Public Citizen, 2015). Currently, host-States are still prone to bear the high cost of international arbitration even when it comes to frivolous claims.

I. Conclusion

As of today, heated debates concerning ISDS are still ongoing. Australia might have finally conceded to ISDS's inclusion in TPPA, but this does not prove that other countries will be as easily compromised (Simmons, 2015).

In respect to Indonesia, as discussed above, at least three of Indonesia's main concerns over ISDS mechanism, which are the scope of covered investment, the scope of consent to arbitration, and distinction between what constitutes as regulatory measure and expropriation, are not exactly consoled by TPPA.

Meanwhile, the other notable provisions in regard to TPPA's ISDS, such as code of ethics on arbitrators, possibility of appellate mechanism, as well as the provision regarding cost of arbitrations and frivolous claims, provide too little – if not at all – consolations over host-States' general concern over ISDS.

Obviously, there are other provisions within TPPA's investment chapter, as well as its ISDS provisions that may be worth to examine to determine whether Indonesia should join TPPA based exclusively on its investment chapter. Nevertheless, based on the limited findings of the Authors, presently the TPPA falls short of consoling Indonesia's concern over ISDS.

For that reason, if Indonesia either terminates, let lapse or renegotiates all of its BITs, up to the point that will perhaps greatly benefit Indonesia as a host-State, it would be regrettable to sign the TPPA, which would only pull back Indonesia to square one; to face the same old concerns over ISDS all over again.

Ultimately, as premised in the introduction, in answering whether Indonesia should join TPP, due considerations are to be given to the other parts of the agreement, aside of the investment chapter and its ISDS provision. Correspondingly, Indonesia should look out elsewhere than the investment chapter in TPP to find more reasons – stronger reasons – to be part of this potentially largest free trade in the world

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