

Report

1 Using developments in international investment protection as an opportunity

International investment contributes to economic growth and prosperity. This is especially true in the case of Switzerland, with its limited domestic market. Foreign investment allows companies to tap into the economies of scale and benefits of networking that frequently play a crucial role in terms of competitiveness.

With direct investment abroad in excess of CHF 1120 billion, Switzerland is among the world's ten largest capital exporters. It is therefore in Switzerland's interest to create favourable conditions for foreign investment. Bilateral investment treaties (BITs) play a key role here. Complementing the national legislation of the host state, they give investors additional legal certainty and protection against political risks. This meets a need when it comes to foreign investment, which typically necessitates tying up assets over the long term in a jurisdiction outside the home state.

BITs – and, more specifically, the investor-state dispute settlement proceedings they provide for – have come under increasing criticism in recent years. Individual states have begun to terminate their BITs – including treaties with Switzerland. Recognising the need for reform in certain areas, Switzerland has in recent years continually enhanced its contractual practice and actively participated in multilateral efforts to draw up new transparency rules for investor-state dispute settlement proceedings.

The investment protection system is also to be further modified in future to make it more efficient and reinforce international acceptance of BITs. Switzerland favours multilateral processes, as they offer the best scope for developing broad-based solutions. Current discussions are focusing on the creation of a permanent multilateral investment arbitral tribunal and an appeal body to replace today's ad hoc courts of appeal. Switzerland is also pursuing the gradual renewal of its BITs.

Against the backdrop of the increasing globalisation of value chains and the digitalisation of the economy, achieving greater legal certainty through investment protection remains of vital importance. At the same time, BITs need to factor in policy coherence, support a development-friendly investment regime (above all in developing and emerging countries) and contribute to the achievement of sustainable development goals.

1.1 Economic significance of international investment

Switzerland owes its successful economic development to attractive conditions allowing companies to invest and create jobs. In the case of Switzerland with its relatively small domestic market, access to foreign sales and procurement markets is particularly important,

as is direct investment¹. The accompanying transfer of technology and know-how is a key driver of competitiveness, prompting countries to deliver conditions conducive to attracting investment from the home market and abroad (infrastructure, education, job market, etc.). This has become all the more significant as technological progress and the dismantling of trade barriers progressively usher in the globalisation of value chains.² Production processes are being subdivided into more and more individual steps to be carried out by different actors in various countries. Multinational companies building up international production and distribution networks through investment abroad play a central role

Cross-border investment has gained substantially in significance since 2000, exceeding growth in the trade of goods.³ The share of developing and emerging countries in global direct investment has increased considerably within just a few years. Flows of international direct investments to developing and emerging economies reached USD 574 billion in 2010, accounting for more than 50 per cent of the global total for the first time.⁴ Over the past ten years, foreign direct investment in Africa increased by approximately the same percentage (8%) p.a. as in North America or Europe. Average annual growth in Asia and Latin America for the same period was even higher, amounting to 12 and 10 per cent respectively. At the same time, developing and emerging countries (such as China, India and Brazil) were beginning increasingly to invest abroad.

Demand for international investment to support sustainable development remains very high. In September 2015, the 193 member states of the United Nations adopted Agenda 2030, containing the global Sustainable Development Goals (SDGs). The plan of action states that these goals can only be achieved with additional investment, while United Nations estimates put developing nations' annual investment requirements in the next 15 years at around USD 2.5 trillion. Besides national and international development efforts and a stable international financial system, private investment is crucial – and international investment in particular. From a development policy perspective, investments will have a sustainable and positive widespread impact, especially when they are embedded in a stable, growth-promoting participatory environment and are undertaken responsibly. This can prevent the creation of isolated pockets of foreign investment that have little tie-in with the local economy and also stimulate balanced growth.

Effects of digitalisation on international investment

The spread of digitalisation is changing business and the working world.⁵ The trigger and basis of this transformation are new information and communication technologies as well as increasingly efficient computer and network infrastructures. Technological advances open up

¹ Direct investment refers to capital investments made by an investor to exercise a direct and lasting influence on the business activities of a company. A direct investment is included in the Swiss National Bank statistics when an investor holds at least 10 per cent of the voting capital of a company or establishes a subsidiary or branch abroad.

² See Foreign Economic Policy Report 2014 (Section 1), BBI 2015 1474.

³ See Wirtschaftliche Bedeutung der Freihandelsabkommen für die Schweiz (Economic Significance of Free Trade Agreements for Switzerland), SECO 2016, available in German, downloadable from: www.seco.admin.ch > Foreign Trade and Economic Cooperation > Free Trade Agreements > Economic Consequences of Free Trade agreements.

⁴ See UNCTAD World Investment Report 2011, p. 2. The report was published in English on the UNCTAD website: www.investmentpolicyhub.unctad.org > Publications.

⁵ See Bericht über die zentralen Rahmenbedingungen für die digitale Wirtschaft (Report on the Framework Conditions of the Digital Economy), SECO 2017, available in German, downloadable from: www.seco.admin.ch > Wirtschaftslage & Wirtschaftspolitik > Wirtschaftspolitik > Digitalisierung.

new possibilities to access foreign markets. They provide opportunities for entrepreneurial innovation as well as novel products, services and business models. Greater digitalisation of production processes allows multinationals to shorten global value chains. It can also enable small and medium-sized enterprises (SMEs) to significantly increase efficiency, for example through facilitated payment operations, new collaboration and marketing models and the use of cloud-based services. Crowd-funding and other alternative mechanisms for raising capital are presenting themselves as complements to traditional forms of financing. At the same time, data privacy is becoming more critical with the advance of digitalisation.

The digitalisation of the economy is also changing global investment patterns. The United Nations Conference on Trade and Development (UNCTAD) examined this phenomenon in its latest investment report⁶, looking at the world's top 100 multinationals. Between 2010 and 2015, the assets of digital and tech multinationals⁷ increased by 65 per cent and their employees and operating revenues by about 30 per cent, representing much stronger growth compared against flat trends for the other multinationals in the same period. All multinationals witnessed a steady rise in the digitalisation of value chains and the share of services in the value of the final product (e.g. in the areas of development or IT), but the increase was particularly pronounced in the case of digital companies. While an average of 65 per cent of the assets of the other multinationals are located abroad and these companies generate 65 per cent of their sales in foreign countries, digital and tech multinationals post over 70 per cent of their turnover outside their domestic market with only 40 per cent of their assets based outside their home country. Therefore, they can reach foreign markets with fewer investments and personnel abroad. Digitalisation is also accompanied by a further shift in the location factors relevant for international investment. The significance of income levels, for example, is likely to dwindle, whereas educational standards will gain in importance.

Significance of international investment for Switzerland

International investment is of prime significance for Switzerland. According to Swiss National Bank (SNB) statistics,⁸ Swiss direct investment abroad (over CHF 1120 billion as at end-2015) and the number of people employed by Swiss-controlled subsidiaries abroad (approx. 2 million) are record figures on an international comparison.⁹ The volume of Swiss direct investment abroad has trebled since 2000. In 2015, direct investment abroad generated capital income of some CHF 92 billion net for Switzerland. Conversely, foreign direct investment in Switzerland in the same year came to approx. CHF 833 billion, with a headcount of more than 456 000.

In Switzerland, in addition to major multinationals, several hundred SMEs also have substantial investments abroad. Capital stocks in manufacturing abroad totalled CHF 395 billion at end-2015, with the largest share (40 per cent) attributable to the chemicals and plastics category. In the same year, capital stocks in the service sector amounted to CHF 332 billion,

⁶ UNCTAD World Investment Report 2017, pp. 155ff. The report was published in English on the UNCTAD website: www.investmentpolicyhub.unctad.org > Publications.

⁷ UNCTAD defines tech multinationals as companies operating in innovative areas of cutting-edge technology, including electronics, IT and bioengineering. Digital multinationals are companies which build on infrastructure and tools in the field of information and communication technology and which comprise a large number of business models (Internet platforms, electronic business transactions, etc.). Telecommunications does not fall under any of the aforementioned categories.

⁸ See Swiss National Bank, Direct Investment, 2015 edition: www.snb.ch > Publications.

⁹ According to UNCTAD figures, Swiss companies ranked 9th globally in terms of direct investment abroad measured in capital stocks in 2016. See table "FDI outflows as a percentage of gross fixed capital formation", UNCTAD World Investment Report 2017, p. 226.

with banks and insurance companies (50 per cent) and trade (40 per cent) accounting for the largest shares. Capital stocks held by finance and holding companies in subsidiaries abroad came to CHF 393 billion. Foreign investment is a key driver of productivity for the Swiss economy. The economies of scale achieved by establishing production or distribution networks abroad are particularly crucial to Swiss companies, given that their home market is comparatively small. On the other hand, investments from abroad provide additional capital and know-how for Switzerland as a business location.

Switzerland thus has a considerable vested interest in the maximum feasible degree of unhindered, non-discriminatory access to international investment markets. At the same time, there are certain areas – such as critical infrastructures in the transport sector or the energy industry (electricity networks, dams, etc.) or systemically important basic services (e.g. in health and education) – where takeovers by foreign investors would not best serve the overriding public interest. In Switzerland, state ownership, licence requirements and special regulations mean that foreign investment is barely possible in these areas.

1.2 Swiss treaty policy

1.2.1 Bilateral investment treaties

Switzerland's foreign economic policy is aimed at ensuring that Swiss companies are given access to foreign markets on the same terms as their competitors abroad. As a key country of origin of international investment, Switzerland has an interest in creating favourable conditions for the foreign activities of its domestic companies and to provide them with effective legal protection. Bilateral investment treaties (BITs), together with free trade and double taxation agreements, are therefore a mainstay of the Federal Council's foreign economic strategy.¹⁰ The conclusion of such economic treaties has positive consequences for trade flows and international investment.¹¹

Swiss companies are increasingly expanding their international activities. Market size, educational standards, salary levels and available infrastructure are all key factors when deciding on investing abroad. Companies also need a stable, predictable environment (legal certainty, data privacy, etc.) given that they are exposed to the particular risks of foreign legal systems when making generally long-term investments outside their own country of origin. Nevertheless, there are still no comprehensive multilateral rules in place here that are comparable, for instance, with those provided for cross-border trade under the mantle of the World Trade Organization (WTO) (see section 1.2.2). BITs go some way to remedying this by providing additional legal certainty to complement the national legal systems.

Globally, there are currently more than 3200 BITs in place, and the number is increasing. In 2016, 37 new BITs were concluded worldwide, while over the same period 19 BITs ceased to be in force following termination by a contracting state.¹² Even if the various BITs are not identical, as a rule they are similarly structured and cover the same fundamental principles.

¹⁰ See Foreign Economic Policy Report 2011 (Section 1), BBI 2012 827, 853.

¹¹ See Exportpotenziale im Dienstleistungssektor, Strukturberichterstattung 47/4 (Export Potential in the Service Sector, Structural Report 47/4), available in German, SECO 2011, p. 24. The study came to the conclusion that positive effects such as an increase in direct investment manifest all the more clearly, the more economic treaties (double taxation, investment protection and free trade agreements, etc.) have been concluded with a partner state.

¹² UNCTAD World Investment Report 2017, p. 111.

Switzerland has signed 116 BITs, 112 of which are currently in force. 91 of the treaties¹³ provided for an investor-state dispute settlement mechanism. In respect of investment, the free trade agreements concluded by Switzerland are normally restricted to market access and do not contain investment protection provisions. The free trade agreements with Japan, Singapore and South Korea are the exception as they also cover investment protection in addition to market access.

BITs guarantee investors international treaty protection against political risks.¹⁴ The principal standards of protection embodied in the BITs concluded by Switzerland are protection against state discrimination (i.e. national treatment and most-favoured nation treatment), protection against unlawful and insufficiently compensated expropriation, guarantee of fair and equitable treatment, protection against failure to honour sovereign commitments, and protection of the free movement of capital and payments. Under the investor-state dispute settlement proceedings contained in the majority of BITs, investors are entitled – in the event of a violation of the treaty – to initiate dispute settlement proceedings against the host state and sue for compensation (see section 1.2.3).

The BITs concluded by Switzerland only provide protection for investments that were lawfully made, i.e. they satisfy the legal requirements of the host state (see section 1.2.4). Accordingly, investors who fail to comply with the law (e.g. in the case of corruption or tax offences) cannot invoke investment protection.

1.2.2 Multilateral treaties

Various instruments of the Organisation for Economic Co-operation and Development (OECD), which are legally binding on Switzerland as an OECD member, cover individual aspects of investment protection, albeit without a formal enforcement mechanism. Under the Declaration on International Investment and Multinational Enterprises, OECD states mutually undertake not to discriminate against investments made in their territory out of another OECD state (national treatment after establishment). The OECD Codes of Liberalisation of Capital Movements and of Current Invisible Operations also guarantee the possibility of investing in other OECD states (most-favoured nation treatment and national treatment, which can be restricted by national reservations). Efforts by the OECD to conclude a comprehensive multilateral investment treaty failed in 1998.

The multilateral Energy Charter Treaty¹⁵, which Switzerland ratified in 1994, provides sector-specific investment rules for the energy sector. Besides rules on energy trading and transit, the treaty also contains provisions on investor protection and an investor-state dispute settlement mechanism.

Multilateral treaties also form the basis for the investor-state dispute settlement proceedings contained in the BITs (see section 1.2.3). The BITs concluded by Switzerland and most other states do not contain detailed codes of dispute settlement practice, but refer to arbitration

¹³ The BITs without an investor-state dispute settlement mechanism are all older treaties concluded before 1990.

¹⁴ Political risks are also referred to as non-commercial risks, as distinct from commercial risks (e.g. incorrect market assessment, business partner in arrears, etc.).

¹⁵ Energy Charter Treaty of 17 December 1994, entered into force for Switzerland on 16 April 1998, SR 0.730.0.

rules agreed at the multilateral level. The ICSID Convention¹⁶ established under the auspices of the World Bank and the rules of procedure based on it contain comprehensive specifications for the constitution and composition of arbitral tribunals, the sequence of dispute settlement procedures and the enforcement of awards. Each contracting state undertakes to recognise arbitral awards rendered under the ICSID Convention and to satisfy the financial obligations contained in them as it would for legally binding awards made by its own national courts. The dispute settlement rules of the UN Commission on International Trade Law (UNCITRAL), which are also used for commercial arbitration proceedings between private parties, also serve as a basis for investor-state dispute settlement proceedings. Furthermore, the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards¹⁷ agreed under the UNCITRAL is relevant for the enforcement of awards under investor-state dispute settlement proceedings. Contracting states to the New York Convention commit to recognising and enforcing arbitral awards rendered under dispute settlement procedures in other contracting states.

1.2.3 Significance of investor-state dispute settlement proceedings

Companies that invest abroad may face problems which, for various reasons, cannot always be resolved under the host state's national legal system. Those cases which, all over the world, lead to legal action range from insufficiently compensated expropriation, discrimination, and failings in the rule of law (e.g. no due process) to restrictions on international capital movements.¹⁸ In common with the majority of other states, Switzerland has also built an investor-state dispute settlement mechanism into its BITs since the 1990s. This allows the investor to refer a dispute with the host state directly to an independent international arbitral tribunal without the involvement of the investor's home state. The prior consent of the contracting states to place disputes over BIT enforcement under the jurisdiction of an arbitral tribunal is already contained in the treaty itself. The direct right of the investor to bring an action against the host state avoids a situation where, in the event of a dispute, the investor's home state is compelled to invoke diplomatic protection against the host state at the risk of creating a conflict between the two countries.¹⁹

In the event of a dispute, the investor can choose between the national legal process of the host state and investor-state dispute settlement proceedings. Access to an international arbitral tribunal affords investors greater legal protection where, for instance, the host state's national courts offer no guarantee of independence and efficiency. In order to prevent multiple actions, Switzerland's BITs prevent investors from simultaneously bringing the same dispute before a national court and an international tribunal. On the other hand, access to the dispute settlement procedure is not conditional on prior exhaustion of the national legal process, since this would last years and cause a considerable delay in the administration of justice. An investor who opts first for recourse to the national legal process does not lose

¹⁶ Convention of 18 March 1965 on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention), SR 0.975.2.

¹⁷ Convention of 10 June 1958 on the Recognition and Enforcement of Foreign Arbitral Awards, SR 0.277.12.

¹⁸ The investor-state dispute settlement proceedings instigated in 2016 related (among other matters) to the cancellation, refusal or non-renewal of concessions and licenses (10 cases), direct expropriations (7), regulations in the area of renewable energy (6) and tax-related measures (5). See UNCTAD World Investment Report 2017, p. 116.

¹⁹ In this connection, BITs are also said to contribute to the depoliticisation of investment disputes.

access to arbitral jurisdiction, as this would be contrary to the interests of the host states and establish an incentive not to resort to the latter's national courts.

As a rule, Switzerland's BITs permit the investor to choose an arbitration procedure pursuant to the rules of the International Centre for Settlement of Investment Disputes (ICSID) or other arbitral regulations such as the UNCITRAL arbitration rules (see section 1.2.2). In both cases, as an initial step, a mandatory consultation period of six to twelve months is provided for, during which a mutually acceptable solution is to be sought. In the majority of cases, an amicable solution is usually found by the end of this first stage. If a settlement cannot be reached, the investor can demand the establishment of an arbitral tribunal, normally comprising three persons. Both parties each nominate one arbitrator, both of whom jointly select a third person to preside over the tribunal. If they fail to agree, an independent third party (e.g. the ICSID Secretary-General) will make the selection. If the arbitral tribunal establishes a breach of the BIT, it is empowered only to award the investor damages (in the form of a monetary payment). It does not have the authority to review, amend or annul national orders or decrees.

Investor-state dispute settlement cases tended to be quite rare until the early 1990s, but they have increased considerably in number in the last fifteen years. According to UNCTAD statistics²⁰, there were 767 known investor-state dispute settlement cases worldwide in the period 1987-2016. In 2016, UNCTAD counted 62 new cases. This is fewer than in the year before (74), but more than the average for the last ten years (49). Since the statistics only cover publicly known cases, the effective figures are presumably higher. Given that more than 3200 BITs have been concluded worldwide, however, these figures are not particularly high. While 109 states have to date been involved once or more in a dispute settlement case, an arbitration action has never been brought against Switzerland. Between 1987 and 2016, the respondent state won in 36 per cent of cases and the claimant investor in 27 per cent. In 25 per cent of cases, the parties reached a settlement. For other reasons, proceedings were not brought to a conclusion in the remaining 12 per cent of cases.

According to UNCTAD, 24 investor-state dispute settlement cases have been initiated by Swiss investors since 1987, with Switzerland thus ranking tenth²¹ among the home states of claimants. This corresponds approximately to Switzerland's ranking in the statistics for global stocks of foreign investment.²² These cases relate to various business sectors. For example, a Swiss investor active in the goods inspection sector was awarded damages of USD 39 million by an arbitral tribunal because the host state failed to meet its payment obligations arising from a mandate to conduct ship inspections.²³ In another case, a Swiss airport operator whose concession to operate an airport was unlawfully revoked by the host state received damages of USD 30 million.²⁴ The highest damages awarded to date to a Swiss investor in connection with a dispute settlement case (USD 650 million) related to the nationalisation of production facilities in the cement sector.²⁵ In this particular case, the

²⁰ UNCTAD World Investment Report 2017, pp. 114ff.

²¹ UNCTAD World Investment Report 2017, p. 116. Figuring at the top of the rankings are the United States, the Netherlands, the United Kingdom, Germany and Canada.

²² See footnote 9.

²³ *SGS Société Générale de Surveillance SA v. Republic of Paraguay* (ICSID Case No. ARB/07/29). See <https://icsid.worldbank.org> > Search Cases Database > ARB/07/29.

²⁴ *Flughafen Zürich AG and Gestión e Ingeniería IDC S.A. v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB/10/19).

²⁵ *Holcim Limited, Holderfin BV and Caricement BV v. Bolivarian Republic of Venezuela* (ICSID Case No. ARB/09/3).

parties reached a settlement on the amount of damages, obviating the need to conclude arbitration proceedings.

These examples demonstrate the practical significance and efficacy of international arbitration proceedings, including for Swiss investors. However, the high procedural costs mean that investors primarily only have recourse to international arbitral jurisdiction if the sum in dispute is substantial. As a rule, an amicable solution is sought first – or, where possible, the case is submitted to a national court in the host state. Furthermore, investors frequently opt not to initiate dispute settlement proceedings because they fear the negative consequences for their future business activities in the host state.

1.2.4 Criticism and challenges

In terms of scope, BITs are relatively short treaties containing a small number of central protection norms based in part on standard formulations. The limited negotiation effort thus required has allowed countries to build up an extensive network of BITs in a relatively brief time. As a result, some protection provisions are broadly formulated and contain legal terms requiring interpretation. A source of particular criticism is that the frequently invoked provisions on fair and equitable treatment and indirect expropriation are insufficiently defined in the treaties. Critics argue that this could lead to investors interpreting these provisions too broadly and initiating arbitration proceedings against the host state even in cases outside the conventional scope of protection of such provisions, which might in turn deter states from using their regulatory powers. Although many years of arbitral tribunal practice have produced some degree of consensus on how these provisions are to be read, they still leave leeway for interpretation. Consequently, Switzerland – in common with numerous other states – has begun to limit this leeway by incorporating formulations of a more detailed nature into the treaty texts. Furthermore, the right of contracting states to regulate in the public interest is confirmed in a specific provision (see section 1.3.2). When defining standards in greater detail, states frequently resort to formulations and criteria developed by arbitral tribunals over the years. This shows that arbitral tribunals are at pains to curb the over-generous interpretation of BITs. This was confirmed, for example, by a recent arbitral ruling based on a Swiss BIT and relating to cigarette packaging regulations motivated by public health policy.²⁶ Rejecting the claim, the arbitral tribunal upheld the host state's right to regulate by evoking the principles of general international law, even though such a right to regulate is not explicitly mentioned in the BIT in question.

BITs are sometimes criticised for being biased in that they grant investors rights without defining their obligations. This argument can be countered by the fact that Switzerland's BITs explicitly protect lawfully made investments only. Any investor failing to comply with the laws of the host state cannot therefore invoke the protection afforded under a BIT. Investors are required to comply with all laws of the home and host states. Should these obligations be violated, the state can exercise its sovereign power through the available instruments in order to take action against culpable investors (court and administrative proceedings, asset seizures, company closures, etc.). In light of these remedies available to the host state to enforce investors' legal obligations, BITs represent a counterweight to avoid the unlawful or arbitrary treatment of foreign investors. In all activities conducted at home and abroad,

²⁶ Philip Morris Brand Sàrl (Switzerland), Philip Morris Products S.A. (Switzerland) and Abal Hermanos S.A. (Uruguay) v. Oriental Republic of Uruguay (ICSID Case No. ARB/10/7).

investors are also expected not only to fulfil their legal obligations but also to uphold internationally recognised standards of responsible corporate governance. Switzerland actively champions the drafting and promotion of such standards (see section 2) and cites these in its more recent BITs.

Criticism is also levelled at the investor-state dispute settlement proceedings provided for in the BITs, with detractors questioning the democratic legitimacy of the arbitral tribunals. This censure is unjustified inasmuch as the system was created by the states themselves and founded on state treaties subject to democratic control at national level (including parliamentary approval). An international arbitral tribunal cannot encroach upon national sovereignty either, nor can it review, adapt or annul national orders or decrees. Should a BIT be violated, it is empowered solely to award the investor appropriate damages in the form of a monetary payment.

As they can have recourse to an international arbitral tribunal as well as to the national courts, foreign investors may also appear to enjoy favoured status with more rights than domestic investors. Despite this impression, BITs are always based on reciprocity. The same rights to bring an action which a BIT affords to foreign investors in Switzerland, for instance, are also available to Swiss investors in the other contracting state that is party to the BIT. While domestic investors cannot initiate arbitration proceedings against their home state, they are granted this option in the other contracting state.

There is, however, some truth in the criticism that investor-state dispute settlement proceedings are insufficiently transparent. While the ICSID website contains key figures on the arbitral tribunal, sequence and outcome of proceedings conducted under ICSID rules, hardly any information on proceedings under the UNCITRAL rules reaches the public domain. Moreover, the publication of awards under either ICSID or UNCITRAL rules requires the consent of both parties. In some instances this has led to awards not being published, which is conducive neither to legal certainty nor to legislative development. From a Swiss perspective, transparency is fundamental to the effectiveness and acceptance of investor-state dispute settlement proceedings. This applies above all because these proceedings are not between private parties but between private individuals and states, which justifies the public interest. Switzerland thus assumed an active role in drawing up the UNCITRAL Rules on Transparency and, by ratifying the UN Convention on Transparency (Mauritius Convention),²⁷ has also placed Switzerland's existing BITs under the new transparency regime (see section 1.3.2). Under the terms of the Convention, all BITs concluded in future will likewise adopt the Rules on Transparency. This might prove difficult in practice, since various negotiating partners – and developing and emerging countries in particular – still have reservations about the new transparency standards.

The procedure for appointing arbitral tribunals continues to attract criticism. Under today's system, the parties nominate a new arbitral tribunal for each individual dispute (see section 1.2.3), giving rise to assertions that these tribunals are effectively ad hoc. This flexibility offers the advantage that arbitral tribunals can be set up quickly and arbitrators with the necessary specialist expertise nominated. On the other hand, it may erode the coherence of arbitral awards, since each tribunal only judges one specific case and awards do not serve as a precedent for subsequent cases. This effect is reinforced by the absence of an appeals body to review awards and, where necessary, correct them in the interests of standardisation. The arbitrators nominated by the parties sometimes also face accusations of a

²⁷ United Nations Convention of 10 December 2014 on Transparency in Treaty-based Investor-State Arbitration, entered into force for Switzerland on 18 October 2017, SR **0.975.3**.

lack of impartiality or a conflict of interest when they serve as attorneys on other cases. Although Switzerland's experiences with the present system have generally been positive, the country is also open to examining new approaches. One possibility would be a binding code of conduct for arbitrators or a more comprehensive institutional reform. The latter should be multilateral in nature, given the global character of the arbitral jurisdiction. Switzerland therefore welcomes the instigation of a multilateral process to examine the creation of a permanent investment arbitral tribunal (see section 1.3.3).

Above all, the growing number of investor-state dispute settlement proceedings initiated against them and the heavy costs involved have led some states to criticise BITs. Complaints are made that individual actions are pursued solely in order to pressurise governments and thereby prevent unwelcome regulations. The increase in dispute settlement proceedings alone is not an indicator of a more aggressive recourse to legal remedies by investors, since the number of such proceedings has not risen disproportionately to the growth in global investment flows. As with any legal system, however, there is always the possibility that the remedies provided for in the BITs may be used improperly. Even if an action is ultimately rejected, each case incurs costs and ties up resources. Switzerland aims to prevent such unjustified or even improper legal actions being brought. Current ICSID rules already give states recourse to abridged proceedings to demand the rejection of manifestly improper actions. Switzerland's new contractual practice (see section 1.3.2) allows for such a review of admissibility under all dispute settlement proceedings conducted on the basis of a Swiss BIT. Furthermore, the unsuccessful party will generally bear the entire costs of the dispute settlement proceedings (costs are presently apportioned at the discretion of the arbitral tribunal). The new regulation on costs is designed to prevent investors from bringing improper actions.

1.3 Enhancing investment protection

1.3.1 Switzerland's objectives

Insofar as criticism of individual aspects of the BITs is justified, Switzerland acknowledges a need for reform and is continually working at various levels to enhance the treaties and provide more effective protection for foreign investments under international law, as well as reinforce global acceptance of BITs.

The objective of enhancing the BITs is to increase legal certainty and foreseeability for investors and host states. At the same time, the current level of investment protection is to be maintained. It is crucial to Switzerland's appeal as a business location that the extensive BIT network should remain in place and Swiss investors enjoy the same standards of protection as their competitors in other countries. Investor-state dispute settlement proceedings are a key factor here. Even though experience shows that the majority of investment disputes are resolved amicably or before national courts, access to an independent international dispute settlement mechanism is vital if international investors are to enjoy adequate legal protection where national legal systems are insufficiently autonomous or impartial. Switzerland's ef-

forts to enhance its BITs are aligned with international developments, most importantly to new EU contractual practice²⁸.

Switzerland factors in policy coherence when concluding BITs, ensuring that the objectives of investment protection are compatible with the SDGs and the interests of developing countries.

1.3.2 Adaptations to date

In recent years, several international organisations (OECD, UNCTAD, UNCITRAL, etc.) have undertaken wide-scale groundwork to help bring about a better understanding of existing BITs and arbitral tribunal practice and have also highlighted various ways to enhance treaties. Switzerland is actively engaged in these multilateral efforts, which form the basis for the adaptation of BITs.

Enhancing BIT contractual practice of Switzerland

Based on the work done in international expert committees, Switzerland has over the past few years continually endeavoured to enhance BIT contractual practice. In 2012, a Federal Administration working group drafted new contractual provisions to reinforce the coherence between BITs and the objective of sustainable development. References to sustainable development, anti-bribery measures, human rights, responsible corporate governance and mutual policy support were added to the preamble. A new BIT provision stipulated that the international health, safety and environment (HSE) protection standards provided for must not be lowered in order to create an incentive for investment. A further new BIT provision expressly confirms the right of contracting states to issue regulations in the public interest (e.g. HSE safeguards), while remaining bound to the general principles of the treaty, namely, non-discrimination and proportionality. The aim of these provisions is to ensure that BITs do not limit states' political latitude to protect public interests. Developing countries in particular have some regulatory ground to make good (e.g. environmental protection) and so are attempting not only to promote direct investment, but to regulate it more stringently. BITs should not have the effect of preventing this.

In 2015, another working group within the Federal Administration was set up to address the question of BITs. Protection standards and investor-state dispute settlement provisions were placed under close scrutiny, using the new EU contractual practice as a potential benchmark. The Report of the Working Group of 7 March 2016²⁹ contains new approaches for various provisions. The duty to ensure fair and equitable treatment is illustrated with examples of actions which contravene this standard. These include the denial of justice in court and administrative proceedings, manifest arbitrariness or improper treatment of foreign investors. Similarly, the provision on indirect expropriation is supplemented with a list of criteria (e.g. economic consequences, discriminatory specifications and duration of a measure) to be

²⁸ On entry into force of the Treaty of Lisbon in 2009, the EU was also given the authority to conclude investment treaties in the area of investment protection. Thus, for instance, an extensive investment chapter regulating market access and protection for investments (including investor-state dispute settlement proceedings) was drawn up under the Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada.

²⁹ Report of the Working Group on BITs of 7 March 2016, available in German at: www.seco.admin.ch > Foreign Trade and Economic Cooperation > International Investments > Switzerland's Investment Treaty Policy

applied when conducting a review to determine in specific cases whether measures implemented by the state constitute indirect expropriation. The explicit inclusion of such "concretisations" in the treaty text helps to avoid excessively broad interpretations in future dispute settlement proceedings and ensures greater legal certainty for host states and investors. Since the aforementioned concretisations correspond substantively to previous Swiss contractual practice, there is no immediate need to renegotiate all of Switzerland's existing BITs, as they can instead be successively amended when the available resources permit (see section 1.3.3).

In respect of the rules of procedure for investor-state dispute settlement proceedings, Swiss BITs restrict themselves to the key benchmarks. Switzerland follows the view that it is generally sufficient to refer to existing multilateral arbitration rules (e.g. ICSID, UNCITRAL, see section 1.2.2), since any repetition or substantial addition to these established regulations serves no useful purpose and could lead to contradictions. This notwithstanding, additional provisions have been elaborated in greater detail for individual key points, including a provision to prevent improper actions being brought, which is designed to permit the rejection of manifestly inadmissible or unfounded claims in abridged proceedings. Furthermore, a new cost regulation stipulates that the unsuccessful party will as a rule bear the entire costs of the proceedings.

UNCITRAL Rules on Transparency

To increase the transparency of investor-state dispute settlement, UNCITRAL drew up new rules on transparency which entered into force on 1 April 2014. These rules provide that all key procedural documents, such as the notice of arbitration, written submissions by the parties and orders and awards of the arbitral tribunal, shall be made available to the public. Hearings of the arbitral tribunal are also, in principle, public. Furthermore, non-disputing parties (third parties) are allowed to file written statements (so-called *amicus curiae* submissions) with the arbitral tribunal. Confidential information (e.g. business secrets) is protected under the rules and exempted from the transparency requirement.

The UNCITRAL Rules on Transparency are automatically applied to investor-state dispute settlements initiated under the UNCITRAL Arbitration Rules pursuant to a BIT concluded on or after 1 April 2014. In the case of investor-state dispute settlements initiated under the UNCITRAL Arbitration Rules pursuant to a treaty concluded before 1 April 2014 or under other arbitration rules (e.g. ICSID), the UNCITRAL Rules of Transparency shall only apply if either the parties to a dispute settlement or the parties to the BIT agree to their application. To facilitate a subsequent agreement between the contracting parties of existing BITs, the UN Convention on Transparency³⁰ was adopted in 2014 and came into force on 18 October 2017. Accession to this Convention means that the Rules on Transparency will be extended to dispute settlement proceedings based on BITs concluded by signatory states of the Convention before 1 April 2014 or conducted under such treaties pursuant to arbitral regulations other than the UNCITRAL Arbitration Rules (e.g. ICSID Rules). Accordingly, not all existing BITs need to be amended individually.

Switzerland was involved in the drafting of the rules of transparency and the negotiations on the UN Convention on Transparency; it ratified the latter (as the third state to do so) on 18 April 2017.³¹ Since 2014 Switzerland has been using a contractual provision for all BITs that stipulates application of the UNCITRAL Rules on Transparency to all arbitration pro-

³⁰ SR 0.975.3

³¹ See Federal Council Report to the Parliament of 20 April 2016 on Ratification of the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration, BBl 2016 4065ff.

ceedings. The BIT between Switzerland and Georgia³², which entered into force on 17 April 2015, is the first BIT in Switzerland (and at the same time the first BIT worldwide) to contain such a provision.

1.3.3 Keys areas of activity for the future

Switzerland is working for reforms at two levels: At the one level, it wants to ensure that the basis of negotiation for the conclusion of new BITs is regularly aligned with international developments. Accordingly, Switzerland has continually modified its negotiation stance in recent years and will do so in future too (see section 1.3.2). At the other level, the question arises as to how existing BITs which no longer meet current standards can be brought into line with these developments. As illustrated below, various mutually complementary courses of action are open.

Renegotiation or revision of BITs

Switzerland concludes new BITs either to replace existing treaties with new ones or to close gaps in the treaty network (see section 8.1.1). Switzerland is currently conducting negotiations with various partner states (e.g. Mexico and Malaysia) to replace older BITs with new treaties. Negotiations with new partners (e.g. Bahrain) presently play a secondary role as only few gaps remain in Switzerland's treaty network. Given that in recent years four states (South Africa, Indonesia, India, Ecuador) have opted to terminate their BITs with Switzerland and other countries, new gaps have arisen. In order to redress the ensuing legal uncertainty, Switzerland aims to conclude new BITs with these states.

The conclusion of new BITs or the revision of existing ones is much more complex than in the past and can sometimes require more time and resources. This is because the majority of states today can draw on broader contractual practice and, in negotiations, often factor-in their experience from previous dispute settlement proceedings based on BITs with other contracting partners. A possible alternative to a wide-scale revision of treaties would be to merely replace individual provisions that are in need of revision. However, experience has shown that negotiations of this nature tend to turn into extensive renegotiations.

Thus Switzerland's contractual network of almost 120 BITs that has grown up over 30 years is to be gradually renewed as the available resources permit. The prioritisation of negotiating partners will be based on the following criteria in particular: economic significance of the partner state; need for additional legal protection for Swiss investors (e.g. if there is no BIT in place, or only a patchy treaty); desire or willingness on the part of the partner state to negotiate; and synergies that can be expected from concurrent negotiations on free trade agreements. Such synergies may arise from the momentum generated by parallel negotiations on a free trade agreement or from the fact that the same delegates are participating in both sets of negotiations and so saving on resources.

When engaging in renegotiations, Switzerland attaches importance to coherence between the BITs and other policy areas as well as to SDGs. Although BITs are special treaties serving the protection of international investments, every effort must be made during negotiations and application to ensure that other political goals are not sacrificed for the sake of safeguarding investment. BITs must, for example, be compatible with SDGs. In concrete terms, this means that an arbitral tribunal must consider the different political aims and weigh them up

32 SR 0.975.236.0

against one another when applying and interpreting a BIT. To reinforce policy coherence and emphasise the significance of this concept for international investments, BITs may allude to relevant global frameworks of reference such as Agenda 2030 for Sustainable Development, SDGs and standards of responsible business conduct.

Joint declarations of the contracting states

By adopting a common treaty interpretation in the form of a joint public declaration, the contracting states can concretise the meaning of individual provisions. This is a convenient way to explain the intent of a treaty, since no formal adaptation is required. However, it does not permit any change to the content of the provisions. This approach may prove expedient where the contracting parties agree on the necessity to concretise individual provisions and there is no need for an extensive revision of the treaty. If a treaty explicitly provides that such interpretations are binding on arbitral tribunals, they will have a direct legal effect. Otherwise, arbitral tribunals can exercise discretion in how they follow these interpretations along with other aspects of treaty interpretation. While such treaty interpretations are currently not explicitly provided for in Switzerland's BITs, it might include this option in future treaties. With respect to existing BITs, Switzerland will also examine from case to case whether, especially as a temporary measure, a treaty interpretation could be used instead of a treaty revision.

Multilateral processes

Since the investor-state dispute settlement mechanism is largely based on multilateral treaties such as the ICSID Convention (see section 1.2.2), reform endeavours should primarily be at this level. Moreover, successful multilateral processes whose findings are applied to numerous states and treaties are more efficient than the adaptation of individual BITs.

This is illustrated by the new UNCITRAL Rules on Transparency, which today are enjoying wide and growing acceptance since they grew out of an open and universal negotiation process. The parties to BITs can refer to these multilateral rules in new BITs instead of expending resources on drawing up separate rules. In one fell swoop, the UN Convention on Transparency (see section 1.3.2) places all the existing BITs of signatory states under the new transparency rules without the need to amend these treaties individually. Collective efforts of this kind make it relatively simple to extend adaptations to existing treaties as well.

In 2016, a process was launched at the initiative of the EU and Canada to look into a comprehensive institutional reform of investor-state dispute settlement proceedings. This includes examining the creation of a permanent multilateral investment arbitral tribunal and an appeal body to be appointed by the member states instead of today's ad hoc arbitral tribunals (see section 1.2.3). Under today's practice, arbitral awards are final and can only be appealed in the event of specific procedural errors. A permanent institution with an appeal option could, therefore, result in a more uniform interpretation of BITs and greater legal certainty for investors and contracting states. Underlining Switzerland's support for this process, the Swiss government hosted an expert group meeting jointly with UNCITRAL in Geneva in March 2017. As a consequence, in July UNCITRAL mandated a working group to carry out further groundwork in preparation for the start of a negotiation process in 2018.

UNCTAD is analysing the impact of BITs on developing countries and helping to establish local specialist expertise and capacity there. Switzerland is actively engaged in these multilateral projects, which are designed to support developing nations in building up the capacity needed for BIT negotiations as well as in investor-state dispute settlement proceedings initiated against them.

1.4

Conclusion

International investments are crucial for the economic development of Switzerland and its partner states. However, foreign investment frequently entails considerable political risks. The international guarantees and enforcement mechanisms embodied in BITs are a key instrument for reducing these risks. Investor-state dispute settlement proceedings have also proven effective in practice. Various applications attest to the practical significance of these proceedings for Swiss investors. Due to the high procedural costs, however, they are usually adopted only as a last resort and only if the sum in dispute is substantial.

While the criticism of international investment protection is only justified in part, there is potential for improvement in some areas. Switzerland has initiated diverse measures to enhance international investment protection as well as increase international acceptance. To this end, efforts are directed at fleshing out the key protection provisions contained in the BITs and increasing legal certainty and foreseeability in the application of the treaties. Investor-state dispute settlement proceedings are also to be improved through transparency, the avoidance of conflicts of interest, and increased institutionalisation. Multilateral processes in particular are suitable for implementing improvements by means of broad-based solutions. Switzerland attaches the utmost priority to multilateral engagement, but also remains committed to moving forward with the gradual renewal of its existing network of BITs.

Against the backdrop of the increasing globalisation of value chains and the digitalisation of the economy, achieving greater legal certainty (e.g. in the area of data privacy) through investment protection is of vital importance. At the same time, BITs must allow for policy coherence and political latitude. This applies in particular with regard to developing nations, where a development-friendly investment regime and the achievement of SDGs should not be impaired.