# International arbitration

Looking ahead to
the top trends in 2019

Freshfields Bruckhaus Deringer

# Welcome to our annual international arbitration top trends publication for 2019.

We have identified the key trends that we expect to dominate the arbitration landscape for the coming year.

Arbitration faced one of its toughest years yet in 2018, particularly in the investor-State sphere. The challenges (and opportunities) of addressing the changing legal, political and economic environment in which we and our clients operate provide some insight into what we can expect to see in the year ahead. We highlight a few examples here:

- The investor-State dispute settlement regime is undergoing something of a re-design, in response to the criticism it has received regarding its fairness. This is manifesting itself in the form of a push to replace traditional treaty arbitration with an investment court system in the EU and other parts of the world, a drive by some States to abandon altogether or to renegotiate their bilateral investment treaties (BITs), and efforts by various bodies to propose ISDS reforms, including a wholesale review of the ICSID arbitration rules. Notably, in the US, Trump's protectionist – and anti-ISDS – agenda has led to a significant reduction in the level of protection enjoyed by investors in the NAFTA replacement, the USMCA.

- Following the March 2018 decision of the CJEU in the *Achmea* case – which ruled that investor-State arbitration provisions in intra-EU BITs are invalid – the future conduct of arbitrations under intra-EU BITs and under the ECT remains unclear. While investment tribunals on such cases have so far ruled that *Achmea* does not affect their jurisdiction, a key question for 2019 is whether EU courts will be prepared to enforce such awards. On the political side, the fall-out from *Achmea* and active lobbying by the European Commission have led all 28 current EU Member States to pledge to terminate their intra-EU BITs.

- The robust legal framework for arbitration and enforcement of arbitral awards in London under the Arbitration Act 1996 and New York Convention will remain unchanged after Brexit, as will the other key features that commend London as an arbitral seat. Indeed, given the uncertainty of the *Achmea* decision on intra-EU BITs, a post-Brexit UK would be an attractive location to structure investments into the EU given its broad network of treaties with EU Member States. There is continuing uncertainty, however, surrounding the future framework for enforcing English court judgments within the EU, and vice versa – meaning that parties may turn to arbitration as a safe harbour to avoid Brexit-related enforcement risk.

- Arbitration funding is becoming increasingly mainstream and the arbitration community is playing catch-up in trying to identify guiding principles to govern its use in arbitration proceedings. A degree of consensus appears to be emerging over the required disclosure of the existence of funding, but not the funding agreement itself.

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We have identified the key trends that we expect to dominate the arbitration landscape for the coming year.

- The shifting balance of economic and political power from Western States to emerging economies looks set to continue in 2019 with an increasing focus on investor responsibility as the counterpoint to investment protection. Recently drafted BITs explicitly prescribe commitments regarding human rights, corporate social responsibility and sustainable development, and arbitral tribunals are starting to take investor conduct into account in determining the level of damages.
- The energy sector is expected to continue to generate a large number of high-stakes disputes between investors and States – in particular in relation to opportunistic 'resource nationalism' in Africa; taxation measures; and recently expired '90s-era production sharing agreements (as States often seek to extract final value from a departing international oil company handing over depleted assets). In the telecoms sector, we foresee an increase in disputes as 'spectrum value extraction' measures – reminiscent of the sorts of 'resource nationalism' measures we have seen in the energy sector over the years – increase.
- Cyber security and data protection issues present a particular challenge to the practice of international arbitration, given that sensitive information is frequently exchanged between multiple entities across borders in any international dispute. While the arbitration community is taking encouraging steps to promote measures designed to assist cyber security and data protection during the course of proceedings, we expect this to be an area that will become increasingly central to – and a contentious part of – arbitrations going forward. Clients should be alive to the risks, as well as the steps that can be taken to minimise disagreement with counterparties over these issues.

As the arbitration system evolves to adapt and respond to the changes that are taking place, our 160-lawyer-strong arbitration practice will continue to participate actively in these processes. Our clients are among the main users of international arbitration and we are firmly committed to improving the process to meet their needs. As international arbitration becomes more sophisticated, an increasing variety of procedural choices are available to parties to resolve their disputes more efficiently. Our promise to our clients is to guide them smoothly and successfully in this evolving environment.

If you would like to find out more about any of these topics, please contact one of us or another of our colleagues in the international arbitration group.


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# 01 Re-designing investor-State dispute settlement

The last few years have seen investor-State dispute settlement, or ISDS, come under increasing attack from multiple quarters.

Accusations have included that ISDS is biased towards investors, that it resolves cases with significant public policy implications in 'secret', that it encroaches too far on the regulatory sovereignty of States, that it too often produces the wrong answer, and that it costs too much and takes too long. These and other criticisms have led to a number of reform processes that are now underway and which will continue throughout 2019.

First is Working Group III (WGIII) of the United Nations Commission for International Trade Law (UNCITRAL), which is tasked with considering ISDS reform. At its last 2018 session, WGIII identified its concerns with ISDS and pronounced it ripe for reform. At its April 2019 session, WGIII is expected to propose specific reforms in three main areas: (i) the perceived lack of consistency, predictability and correctness in arbitral awards; (ii) the perceived lack of independence, impartiality and diversity among arbitrators; and (iii) the cost and duration of ISDS proceedings. WGIII is expected to circulate reform proposals before its April session, which might include such recommendations as an appellate system for arbitral awards, new rules on arbitrator appointments and further mechanisms to strike out frivolous claims early in proceedings.

Second is the push of the European Commission (the Commission) to replace arbitration with an investment court system (ICS) to hear claims under treaties to which the EU is party. The Canada-EU Comprehensive Economic and Trade Agreement (CETA) includes the postulated ICS, as do new EU treaties with Singapore, Vietnam and Mexico, but no such court is yet in existence and this aspect of these treaties is not yet effective. Serious questions remain as to exactly how an ICS would work, in particular with respect to the appointment of judges, and some States have expressed doubts about whether an ICS would be consistent with other European treaties. Following Belgium's request in 2017, an opinion of the Court of Justice of the European Union (CJEU) is due imminently regarding the compatibility of an ICS with (i) the exclusive competence of the CJEU to provide the definitive interpretation of European Union law; and (ii) rights of access to the courts and to an independent and impartial judiciary.

Meanwhile, the historic EU-Japan Economic Partnership Agreement that will come into force in February 2019 currently includes no dispute resolution provisions, as the parties are still negotiating between the EU's ICS model and Japan's preference for arbitration. The result of this tussle between the EU and Japan in the context of such a significant treaty might be an indication of the direction of travel more generally.

Third, and in a similar vein, the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) came into force at the end of 2018, and includes traditional – albeit slightly narrowed – ISDS arbitration provisions. However, six of the 11 States that are party to the CPTPP have signed side letters excluding ISDS between themselves, and three signed a declaration stating that they will 'consider evolving international practice and the evolution of ISDS' to determine its future application. For 2019, arbitration is available between some but not all of the States party to the CPTPP, but how long that will last is an open question.

> **'For investments being made now, which may produce disputes long into the future, investors would be wise to ensure as much protection by way of contract as possible, so as to be left less to the vagaries of what may become of ISDS.'**
>
> Ben Juratowitch QC, Partner

Fourth, some States have sought to abandon altogether or to renegotiate their BITs in an effort to address the perceived imbalance of rights and obligations between States and investors in current agreements. Several States – including Bolivia, Brazil, Ecuador, Indonesia, South Africa and Venezuela – have taken steps to reject ISDS other than through their own local courts. The US, Canada and Mexico have abandoned ISDS between the US and Canada, and between Mexico and Canada, in the revised version of the North American Free Trade Agreement (NAFTA),



This article continues on the next page

## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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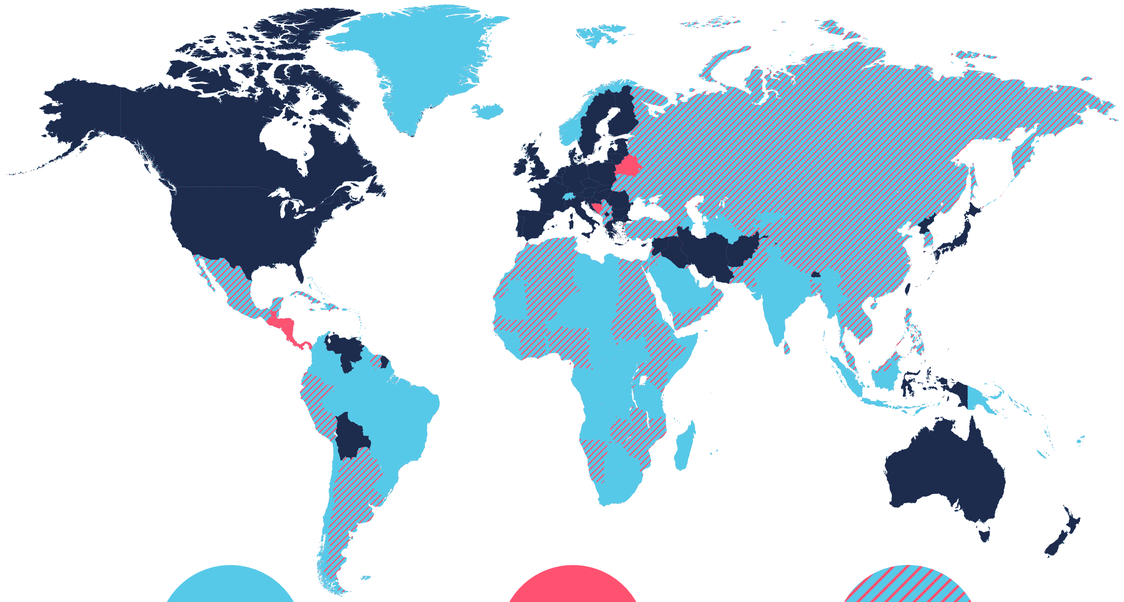
the United States-Mexico-Canada Agreement (USMCA). The Dutch Government, meanwhile, adopted its new Model BIT in October 2018, narrowing the protections to be included in new Dutch BITs, and potentially setting the stage for seeking to renegotiate the 78 BITs it currently has with States outside the EU. The Dutch BITs are among the most significant in existence because of the number of foreign investment vehicles incorporated in the Netherlands. As well as potentially limiting the substantive protections afforded to investors, key changes in the Dutch Model BIT include requiring real business presence in the Netherlands, changing the procedure for the conduct of and access to arbitration, and proposing that an ICS ultimately replace the current ISDS arbitration regime. More States will likely follow the Netherlands' lead in seeking to negotiate a new generation of investment agreements in 2019 and beyond. At the institutional level, we see criticisms of the ISDS system (particularly delay and cost) being addressed in different initiatives such as the WGIII and the ICSID arbitration rules revision process.

Notwithstanding the significant uncertainty surrounding what will become of ISDS over the next few years, for the moment there remains a wide array of investment agreements that continue to provide for meaningful investment protection, including international arbitration between foreign investors and States in which they invest. For disputes arising in the short term, further changes to the system may therefore not be important. For investments being made now, which may produce disputes long into the future, investors would be wise to ensure as much protection by way of contract as possible, so as to be left less to the vagaries of what may become of ISDS.

## The wide-spread impact of ISDS reforms



**54**

States and other entities have an investment treaty in place with the EU and may therefore be affected by the EU's proposed ICS reforms

**78**

non-EU States may be affected by the Netherlands Model BIT

entities affected by both scenarios



## Contents


01 **Re-designing investor-State dispute settlement**

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

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# 02 Trade and investment in the age of Trump

President Trump took office in January 2017 promising to implement his protectionist agenda.

Within 12 months, the US had withdrawn from the negotiations for the Trans-Pacific Partnership (TPP), vowed to renegotiate NAFTA and had put on hold negotiations with the EU on the Transatlantic Trade and Investment Partnership (TTIP).

Trump's 'America First' agenda progressed further in 2018. He was accused of provoking a trade war, following the imposition of punishing tariffs on steel and aluminium in June (including on allies of the US), followed by two rounds of retaliatory tariffs on Chinese goods in July and September. And after fitful negotiations marked by difficult compromises on trade issues, USMCA was signed on 30 November 2018 with the object of replacing the 25-year-old NAFTA (if approved by Congress, its entry into force is expected in 2020). The protections offered by its investment chapter have been significantly curtailed, reflecting the Trump administration's rejection of the US's historically favourable policy towards ISDS. The USMCA's key features are as follows:

- while it provides broad protections to investors, it limits the enforcement of those protections through international arbitration;
- it provides that claims relating to legacy investments can be brought within three years of NAFTA's termination, pursuant to NAFTA's provisions;
- it eliminates ISDS between the US and Canada. In the event of a dispute, US investors in Canada and Canadian investors in the US will be unable to enforce the USMCA's obligations through arbitration, and will instead need to pursue remedies before local courts;
- it eliminates ISDS between Mexico and Canada. However, Mexican and Canadian investors will be able to arbitrate claims under the CPTPP, which was signed in March 2018 by Mexico, Canada and the nine other remaining TPP States. The CPTPP entered into force for Mexico and Canada on 30 December 2018, and provides investment protections that are broadly similar to those of NAFTA;

**'US, Canadian and Mexican investors would be wise to revisit the structure of their investments in the USMCA trade zone to ensure continued protection of their investments.'**

Caroline Richard, Partner



This article continues on the next page

## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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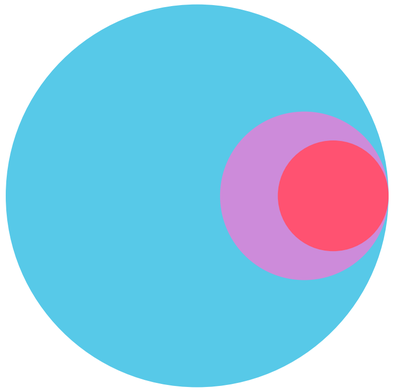
- it provides a stripped-down version of ISDS between the US and Mexico, but only after investors have pursued remedies before local courts for 30 months (unless recourse to domestic remedies is 'obviously futile'). This 'ISDS Lite' limits claims to national treatment, most favoured nation treatment and direct expropriation. However, the US and Mexico can deny the benefits of the USMCA's protections to companies that, while established in the other State party, are in fact owned or controlled by the denying State and have no substantial business activities other than in the denying State; and
- US and Mexican investors that have entered into government contracts in energy, telecoms and infrastructure sectors can bring claims for breaches of all of the USMCA's investment protections, and thus get broader protection, so long as the respondent State is still a party to another investment agreement that contains ISDS.

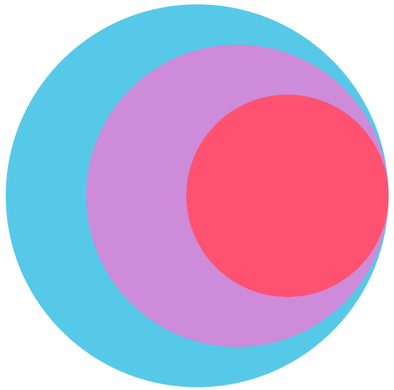
Finally, in October 2018, the US announced its intention to open trade talks with the EU, the UK and Japan. The USMCA provides a blueprint for the trade and investment terms likely to be sought by the Trump administration. Whether they will be accepted remains to be seen.



## ICSID cases involving the US

- Total ICSID cases: 715*
- Cases by US claimants at ICSID: 139*
- Cases against the US at ICSID: 6*

* Includes pending cases and ICSID Convention and ICSID Additional Facility cases



## NAFTA arbitration cases and the US

- Total NAFTA cases: 61*
- NAFTA cases brought by US investors: 38*
- NAFTA cases brought against the US government: 17*
- NAFTA cases lost by the US government: 0

* Including pending cases



## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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# 03 The future of intra-EU bilateral investment treaties following *Achmea*

On 6 March 2018, the CJEU ruled in *Achmea v Slovak Republic* that (at least under the Germany-Slovakia BIT: the exact scope of the decision will have to be clarified by the CJEU in due course) the Treaty for the operation of the European Union precluded provisions in treaties between EU Member States providing for arbitration by an investor of one Member State against another Member State. Following the CJEU's judgment, the referring court (the German Federal Court of Justice (Bundesgerichtshof)) set the original award aside. In July 2018, the Commission announced that following *Achmea*, all investor-State arbitration clauses in intra-EU BITs 'are inapplicable' and any tribunal established under them 'lacks jurisdiction due to the absence of a valid arbitration agreement'.

Following *Achmea*, we saw respondent States raise arguments before investment treaty tribunals under intra-EU BITs and between EU investors and Member States under the Energy Charter Treaty (ECT) that they lacked jurisdiction. The Commission also launched a persistent campaign to intervene in arbitrations pursued under intra-EU BITs or the ECT (regardless of applicable arbitral rules, and including several in which Freshfields is involved as counsel for the investor), to inform tribunals they lacked jurisdiction.

Despite these efforts, investment treaty tribunals have systematically ruled that *Achmea* does not affect their jurisdiction. In May 2018, an ICSID tribunal in *Masdar v Spain*, an ECT case, ruled that *Achmea* had 'no bearing', and stated that *Achmea* was limited in its application to intra-EU BITs, highlighting that the EU was itself a signatory to the ECT and had thus agreed to its dispute resolution provisions. Similarly in August 2018 in *Vattenfall v Germany*, another ICSID case under the ECT, the tribunal ruled that EU law was not generally applicable to the interpretation and application of arbitration clauses in the ECT. Investment treaty tribunals have been similarly unimpressed with jurisdictional arguments based on *Achmea*. In October 2018, the tribunal in *Group UP and CD Holdings v Hungary*, a claim by a French vendor of food vouchers against Hungary in respect of municipal tax reforms that destroyed its business in that country, ruled that *Achmea* was inapplicable. The tribunal said that *Achmea* did not refer to the ICSID Convention, and that Hungary could not be taken to have renounced the ICSID Convention (the source of the tribunal's jurisdiction) by accession to the EU. We can expect this trend of jurisdictional objections and their rejection by tribunals to continue in 2019.

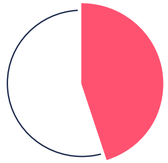
The question in *Achmea* arose from a reference by the court at the seat of the arbitration, Frankfurt am Main, related to Slovakia's unsuccessful argument before the tribunal that it lacked jurisdiction. There is no equivalent national court review of ICSID awards (which are the subject of a self-contained regime under the ICSID Convention) and so no application similar to that which led to the *Achmea* judgement will be possible in such cases. However, all eyes remain fixed

**174**

the number of known treaty-based arbitrations initiated by an investor from one EU Member State against another EU Member State (by 31 July 2018)

**20%**

of the 904 known ISDS cases globally



**45%**

of intra-EU cases are brought pursuant to the ECT

**12**

the number of BITs to which the UK is a party that are currently intra-EU BITs but may soon (post-Brexit) be extra-EU BITs

Source: UNCTAD 'Fact sheet on intra-European Union investor-State arbitration cases' (IIA Issues Note, No 3, December 2018)

This article continues on the next page

Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 **The future of intra-EU bilateral investment treaties following *Achmea***

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

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on the question of whether EU Member State courts will enforce awards rendered by ICSID tribunals constituted under intra-EU BITs that have found jurisdiction. An award that is practically unenforceable in the EU may leave investors hunting for assets of Member States situated in non-EU countries. Indeed, a claimant that obtained a successful ECT award under the SCC Rules is currently seeking recognition of that award in the US federal courts in the *Novenergia v Spain* case. If we turn to the EU, the same claimant seeks recognition and enforcement of its award before the Svea Court of Appeal in Sweden. The same issue applies to *PL Holdings Sàrl v Poland*. In July 2018 the English Court of Appeal in *Micula v Romania* declined to lift a stay of enforcement of an ICSID award under an intra-EU BIT, expressly leaving the question of the effect of *Achmea* open.

The current political climate looks set to feed uncertainty regarding enforcement. On 15 January 2019 (and following similar announcements by some individual Member States, including the Netherlands and Hungary, throughout 2018) a declaration by 22 EU governments pledged to terminate their intra-EU BITs, and to notify tribunals in arbitrations constituted under them of the non-arbitrability of intra-EU BIT and intra-EU ECT claims. Two separate declarations, one by Hungary and one jointly by Finland, Luxembourg, Malta, Slovenia and Sweden, did not join the other 22 governments' position regarding the enforceability of the ECT in relation to intra-EU claims, with the joint five-country declaration expressly reserving the position on the basis of the ongoing litigation before the Svea Court of Appeal. Accordingly, this year we can expect to see further interventions in intra-EU BIT and ECT arbitrations, together with actions to set intra-EU BIT and ECT awards aside in Member State courts (if the seat is in the EU) and to prevent enforcement of such awards within and outside the EU. The position regarding ECT claims remains to be further tested.

A related question for 2019 is what will happen to the 12 intra-EU BITs to which the UK is a party. Depending on the deal (if any) that is reached, such BITs will after Brexit no longer be classified as intra-EU, so will be immune to the jurisdictional and enforcement challenges of *Achmea* – which could provide some welcome certainty for UK-based investors (who currently have 12 known pending investor-State arbitrations against EU Member States) and may well provide a safe haven for EU-based investors who want to keep the possibility of bringing investment treaty claims against EU Member States.

**'The European Union has moved with a perhaps surprising degree of consensus among Western and Eastern European Member States to seek to take advantage of the *Achmea* judgment and block intra-EU investment treaty claims. It will be interesting to see what effect the Member States' declarations has on pending claims (ie, whether tribunals will uphold jurisdiction and whether resulting awards can be enforced within the EU) and whether EU-based investors will continue to bring claims against EU Member States under BITs and the ECT.'**

Peter Turner QC, Partner



## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 **The future of intra-EU bilateral investment treaties following *Achmea***

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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# 04 Arbitration in the age of Brexit

As the uncertainty continues into 2019, one thing is clear: arbitration has an important role to play.

On 29 March 2017 the UK gave notice to leave the EU under Article 50 of the Lisbon Treaty, giving effect to the June 2016 referendum vote and triggering a two-year period of intense negotiations with the EU leading up to the UK's withdrawal. The UK and EU negotiating teams prepared a draft withdrawal agreement establishing a transitional period and a draft political declaration setting out a framework for their future relationship, but the agreement was resoundingly rejected by the UK Parliament on 15 January 2019. As exit day (29 March 2019) fast approaches, a no-deal exit is possible if a viable alternative cannot be found. There are calls for a second referendum (the CJEU recently ruled in the *Wightman* case that the UK can unilaterally revoke its Article 50 notice) and, as an interim step, an extension of Article 50 (which would require the consent of the other EU Member States). At the time of writing, it would take a braver commentator than these authors to predict the outcome.

All of this means that there is continuing uncertainty surrounding the future framework for enforcing English court judgments within the EU, and vice versa.

Parties currently enjoy a smooth enforcement framework across the EU under the Recast Brussels Regulation. On exit day, or at the end of any transitional period if a revised withdrawal deal is ultimately agreed and approved, the UK will need an agreement with the EU to stay within the Recast Brussels regime. Such an agreement looks unlikely, not least because several EU Member States are now establishing English-language courts in order to attract cross-border litigants away from the English courts in the wake of Brexit, on the premise that the UK will no longer benefit from the Recast Brussels regime.

The UK has two alternatives: seek to accede to the Lugano Convention (which appears to be the UK's preferred plan, and a key part of its current negotiation strategy with the EU), which has been ratified by the EU, Switzerland, Norway and Iceland; and/or accede to the Hague Choice of Court Convention, which has been ratified by the EU, Denmark, Montenegro, Mexico and Singapore (China has signed but not yet ratified). These instruments also provide a framework for the enforcement of court judgments. However, neither would be plain-sailing:

a) The UK would need the agreement of all EU Member States (and other signatory States) to accede to the Lugano Convention. If there are political issues that prevent a deal to stay in the Recast Brussels regime, those same issues could be a roadblock to accession to Lugano.

b) The UK can accede unilaterally to the Hague Convention and has made clear that it plans to do so, but that is limited in scope: (i) it is directed at disputes under commercial contracts containing exclusive jurisdiction clauses (non-exclusive jurisdiction clauses and sole option clauses are not protected); (ii) it does not cover orders for interim relief; and (iii) it only applies to English exclusive jurisdiction clauses that are concluded while it is in force in the UK. If there is a gap between exit day and the UK's re-accession to the Convention, contracts concluded during that period may not be protected.



This article continues on the next page

## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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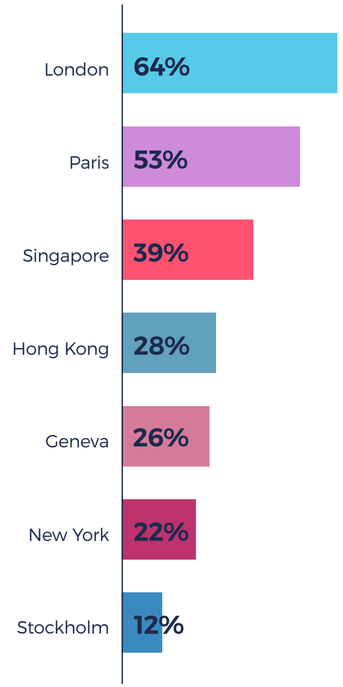
Meanwhile, Brexit will have no impact at all on commercial arbitration. The robust legal framework for arbitration in London under the Arbitration Act 1996 will remain unchanged, as will the other key features that commend London as an arbitral seat, including language and legal culture, skilled counsel and experienced arbitrators, and a supportive and non-interventionist judiciary. Brexit will also have no impact on the enforcement of arbitral awards: UK awards will continue to be enforceable in all remaining EU Member States, and vice versa, under the New York Convention. As noted by our colleagues in the previous section, a post-Brexit UK is likely to become an attractive place through which to structure investments into the EU as its own network of BITs with EU States will not be affected as a consequence of the *Achmea* decision.

Arbitration may also have a role to play in dispute resolution under any withdrawal deal and any future partnership agreement. Under the draft withdrawal agreement that was put to the UK Parliament, any disputes were to be referred to a Joint Committee of EU and UK representatives in the first instance; and if the dispute could not be resolved by the Joint Committee, either side would be entitled to initiate arbitration proceedings. Any questions of EU law were to be referred to the CJEU for a binding ruling. The same dispute resolution mechanism is likely to be adopted in any alternative deal agreed between the UK and EU.

**'As the uncertainty surrounding Brexit continues into 2019 and it remains unclear what framework will apply to the enforcement of UK court judgments, parties may turn to arbitration and the security of the New York Convention as a safe harbour to avoid Brexit-related enforcement risk.'**

Oliver Marsden, Senior Associate

## London remains the preferred seat of arbitration*




*According to the 2018 Queen Mary University of London and White & Case International Arbitration Survey (the 2018 international arbitration survey), p 9, London remains the preferred seat of arbitration despite Brexit concerns. In answer to the question 'What are your or your organisation's most preferred seats?', the percentage of respondents who included the seat in their answer is shown.



## Contents

01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform

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# 05 Third-party funding: emerging norms in an ever-evolving market

Identifying guiding principles for an industry as fast evolving and diverse as arbitration funding is a challenge. But the final report of the ICCA-Queen Mary University Task Force on Third-Party Funding, published in April 2018 (the ICCA Report), nonetheless provides some early indications of the direction of travel, incorporating the perspectives of a broad range of industry stakeholders, including funders and lawyers.

In particular, we might be seeing an emerging consensus regarding the required disclosure of the existence of third-party funding in arbitration proceedings. The ICCA Report recommends that parties and/or their representatives should disclose the existence of a funding arrangement and the identity of the funder and that the tribunal should have the power to order such disclosure. This is driven by a desire to facilitate checks for potential conflicts of interest for arbitrators, which might otherwise call into question the validity of the award. This approach is broadly in line with recently enacted regulatory frameworks in Hong Kong and Singapore, along with the proposed amendments to the ICSID Rules (issued for discussion in 2018 with a view to adoption in 2019/20, if approved), which envision an obligation on the parties to disclose the existence and source of third-party funding.

A universal obligation to disclose might have unintended procedural consequences, however. Will systematic disclosure give rise to new conflict concerns, for instance if an arbitrator becomes aware of repeat appointments where the same funder is involved? Furthermore, in circumstances where it is obvious that there is no risk of conflict of interest (ie the funder is operating at arm's length from the tribunal), will disclosure do no more than provide the respondent with an opportunity to bring a strategic procedural challenge or make further applications for disclosure to delay the proceedings?

In this regard, the extent of disclosure required and the costs consequences of third-party funding remain topics for debate. For example, 2018 saw the second-ever (publicly known) security for costs order in an investment arbitration being granted against a funded claimant in the *Garcia Armas v Venezuela* case.

Freshfields worked on 12 third-party-funded international arbitrations in 2018

**'Third-party funding in international law is regulated by a hodgepodge of national laws, institutional rules and soft law, all of which are constantly evolving. We have the necessary know-how and experience to help our clients navigate this regulatory patchwork.'**

Nick Lingard, Partner



This article continues on the next page

Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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The ICCA Report suggests that the existence of third-party funding should not be a relevant factor in considering applications for security for costs. However, at the same time, the Report notes that, on a case-by-case basis, disclosure of relevant parts of the funding agreement may be needed to reach a decision on an application for security for costs, as tribunals may wish to know whether the funder has agreed to take on liability for adverse costs orders and security for costs orders.

As a general matter, it remains to be seen whether the principles set out in the ICCA Report will catch on as a form of soft law, and also whether it is suited to purpose as the funding market continues to evolve. While the regulatory landscape seeks to standardise, the market seems to be doing just the opposite, with new funding structures being agreed on an ongoing basis. As just one example, the acquisition of a claimant entity (or a funder taking an equity stake in the claimant) is gaining popularity as an alternative to a more traditional arm's length funding relationship.

**'Don't be fooled by references to "market standard" funding structures. Our clients continue to fund their cases through bespoke arrangements. While some funders try to push their preferred terms as "standard", there are a range of negotiation opportunities for the client who stays alert and isn't afraid to dig into the details of funding proposals.'**

Noah Rubins, Partner

According to the 2018 international arbitration survey:

**97%**

of the respondents are aware of third-party funding in international arbitration;

**16%**

have used it in practice; and

the majority have a generally 'positive' perception of it, particularly those who have used it.



## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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# 06 The drive to improve efficiency in arbitral procedure: a success or more to do?

We expect that, in 2019, arbitral institutions, States and practitioners will continue the push to improve efficiency in arbitral procedure.

Nigeria and Sweden are two examples of States expected to follow this trend. In Nigeria, the Arbitration and Conciliation Act (Repeal and Re-enactment) Bill looks set to replace the current Arbitration and Conciliation Act (1988), which is now 30 years old. The Bill is still under debate but if it becomes law in 2019 it will provide for the appointment of emergency arbitrators and the ordering of measures providing interim relief and security for costs. Similarly, proposed amendments to the Swedish Arbitration Act are set to enter into force on 1 March 2019. The amendments aim to increase efficiency and provide, among others, for multiparty arbitrations and the consolidation of similar proceedings where parties consent.

This trend follows a number of countries revising or seeking to revise or update their arbitration laws and provisions during 2018, such as China where the Supreme People's Court released a few judicial interpretations on arbitration in 2018. The judicial interpretations strengthen China's pro-enforcement credentials and underscore that the Supreme People's Court is the final Chinese court empowered to refuse to recognise and enforce arbitral awards – both foreign and selected domestic awards.

A number of arbitration institutions also look likely to issue revised rules aimed at promoting efficiency, following on from the issuing of new rules in 2018 by the German Arbitration Institute (DIS) (in force on 1 March 2018) and Hong Kong International Arbitration Centre (for arbitrations commenced after 1 November 2018).

These include ICSID which has issued a draft new set of Rules for discussion and adoption in 2019/20 (if approved by ICSID Member States), containing amendments and new sections designed to streamline procedure. These include: (i) an expedited procedure; (ii) a reduced and more clearly specified timeline of procedural steps in the arbitration; (iii) a requirement for tribunals to endeavour to issue awards within 240 days of the last submission of the parties (as well as advising parties better in the event of delay); (iv) detailed provisions around applications for bifurcation; and (v) specifying electronic filing as the default method to be used.

Will any of the above lead to greater efficiency in arbitration? We expect so, but it depends on several factors. New laws and institutional rules allowing for emergency arbitrators and expedited procedures give parties options to achieve faster outcomes and avoid

**'We expect that arbitration will become more efficient as a result of the efforts to improve procedure currently being driven by States, arbitral institutions and practitioners. But the success of this movement will depend partly on the willingness of institutions to enforce their own rules and the sanctions they can impose on recalcitrant parties and tribunals.'**

John Choong, Partner



This article continues on the next page

## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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preliminary battles in public courts. More importantly, institutions are giving tribunals better case management powers to ensure more efficiency and themselves better leverage to ensure faster decisions from arbitrators. The success of these measures will depend on the willingness of institutions to enforce their own rules and the sanctions they can impose. For example, the DIS can take a tribunal's procedural efficiency into account when deciding on the costs they will receive whereas ICSID, by contrast, can only compel tribunals to give reasons for delays. There is, nonetheless, value in establishing normative periods for the issuance of awards: arbitrators who fail to meet deadlines may, for example, face difficulty getting repeat appointments.

Aside from changes to arbitration laws and rules, new options for the regime for producing evidence in arbitrations will become available in 2019 following the release of the Prague Rules in December 2018. In summary, the Prague Rules offer an alternative to the IBA Rules and may be voluntarily adopted by parties or tribunals as part of the procedural rules for an arbitration. Having been developed by practitioners who believe the IBA Rules are too biased towards a party-driven, Anglo-Saxon/common law model, the Prague Rules promote an inquisitorial approach that limits document disclosure and witness examination and gives tribunals a more active role in managing the procedure and establishing facts.

It remains to be seen if the Prague Rules will be widely adopted in preference to the well-established IBA Rules. Many doubt this will occur. Given the need for consensus on their adoption, the Prague Rules are more likely to be favoured in arbitrations between parties from civil law jurisdictions where counsel on both sides and the tribunals are more comfortable with civil law procedural norms.

As for procedural efficiency, tribunals adopting the more inquisitorial pro-active approach to procedure advocated by the Prague Rules may achieve some time and cost savings, but – it is argued – there may also be an increased risk that awards may later be challenged by parties who assert their due process right to be heard has been overridden.

According to the 2018 international arbitration survey:

**61%**

of respondents thought that 'increased efficiency, including through technology' will be the factor that has the most significant impact on the future evolution of arbitration; and

**67%**

selected 'cost' as the worst feature of arbitration.



## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 **The drive to improve efficiency in arbitral procedure: a success or more to do?**

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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# 07 The impact of human rights and environmental law on investment treaty arbitration

In 2018, we highlighted the growing relevance of arguments based on international human rights and environmental law to investment treaty arbitration. In 2019, we believe the focus on investor responsibility, as the counterpoint to investment protection, will continue.

Following the 2017 landmark decision in *Urbaser v Argentina*, where the tribunal accepted jurisdiction over Argentina's counterclaim based on the human right to water, tribunals have continued to grapple with arguments raised by States based on alleged violations of human rights and environmental standards. In *Bear Creek Mining Corporation v Peru* (November 2017), for example, the tribunal limited the investor to recovery of its sunk investment costs in circumstances where there was limited prospect of obtaining a 'social license to operate' for a mining project, with the dissenting arbitrator also proposing a further reduction in damages for contributory fault. Meanwhile, in *Aven v Costa Rica* (September 2018), the tribunal upheld Costa Rica's right to enforce environmental regulations and accepted jurisdiction in principle over a counterclaim.

Further reflecting States' increasing public interest concerns, recently drafted BITs explicitly prescribe commitments regarding human rights, corporate social responsibility and sustainable development, alongside protections for investors. For example, on 19 October 2018, the Dutch Government adopted a new Model BIT, which contains an innovative provision that permits investor compensation to be reduced for non-compliance with the UN Guiding Principles and the OECD Guidelines for Multinational Enterprises; it further provides that investors can be liable for damage in the host State under the rules applicable in their own home State. The Dutch Government has announced plans to notify the Commission of its intention to renegotiate its 78 non-EU BITs in line with the new Model BIT. It will be interesting to see how this renegotiation process unfolds and the extent to which the Model BIT may recalibrate States' approach generally to investment protection. Further examples include the Cooperation and Facilitation Investment Agreements that Brazil has signed with Ethiopia (April 2018) and Suriname (May 2018), both of which contain provisions aimed at encouraging sustainable development and corporate social responsibility, as well as provisions expressly confirming that the host State is free to adopt measures in order to ensure that foreign investment is carried out according to national labour, environmental and health laws.

Efforts are also underway to develop a legally binding UN instrument that sets out the rights and obligations of transnational corporations in relation to human rights, as well as to develop a set of arbitral rules specifically tailored towards the resolution of disputes concerning alleged violations by multinational enterprises.

> **'States are increasingly invoking human rights and environmental obligations as a potential "shield" against claims by investors. One question is whether we will see such obligations used by States as a possible "sword".'**
>
> Will Thomas, Partner



This article continues on the next page

## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 **The impact of human rights and environmental law on investment treaty arbitration**

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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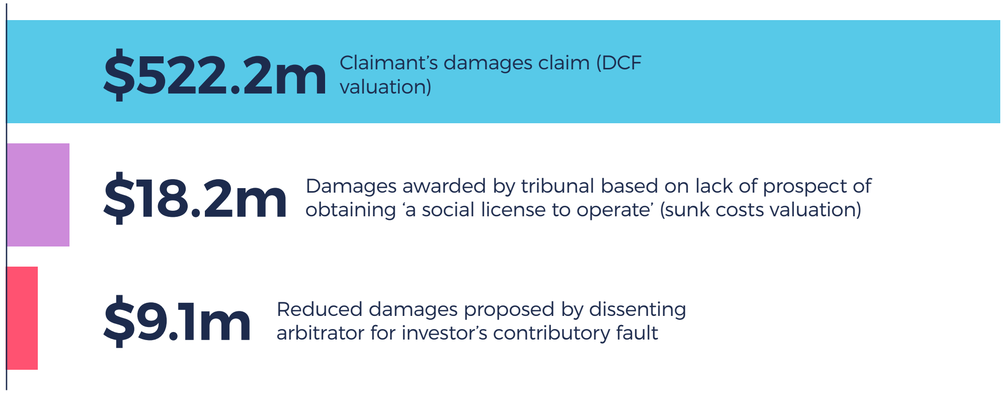
## Climate change

Climate change will remain firmly on the global agenda in 2019, with the number of disputes set to rise. Arbitration is likely to play an increasingly significant role in the resolution of these disputes, particularly in determining how the financial risks associated with climate change should be allocated.

With energy transition predicted to cost trillions of dollars annually, questions will inevitably arise as to who should shoulder the fiscal burden. In the recently commenced NAFTA case of *Westmoreland Coal Company v Canada* (November 2018), for example, the investor does not dispute Alberta's decision to tackle climate change by accelerating the phase-out of coal-fired power utilities, but rather objects to Alberta's refusal to lessen the financial burden of that decision through compensation in accordance with NAFTA.

As such disputes become more common, it appears likely that both investors and States will raise increasingly innovative arguments relating to climate change. We will watch with interest to see how these arguments are treated by tribunals; what seems certain is that climate change will have an ever more important impact not only on the interpretation of investment treaty standards, but also on our evolving appreciation of investor responsibility.

*Bear Creek Mining Corporation v Peru* [2017] – the impact of human rights arguments on the recovery of damages






## Contents

01 Re-designing investor-State dispute settlement
02 Trade and investment in the age of Trump
03 The future of intra-EU bilateral investment treaties following *Achmea*
04 Arbitration in the age of Brexit
05 Third-party funding: emerging norms in an ever-evolving market
06 The drive to improve efficiency in arbitral procedure: a success or more to do?
07 The impact of human rights and environmental law on investment treaty arbitration
08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?
09 Cyber security and data protection in arbitration: too important to ignore
10 The legitimacy of the arbitration process: ongoing debate and reform

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# 08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

The energy and telecoms sectors – involving as they do an intersection between high volumes of foreign investment, scarce national and natural resources and a perception of significant profits being siphoned off abroad – continue to generate a large number of high-stakes investor-State disputes.

To follow up on a regional trend highlighted in last year's issue, opportunistic 'resource nationalism' in Africa continues its incline. The statistics published by ICSID show that Africa has replaced Central and South America as the dominant region for investor-State claims in 2018 – with approximately half these disputes involving energy or telecoms.

Over the last six months, Nigeria has embodied this trend, having taken aggressive measures against investors in (i) the oil and gas sector (where the Supreme Court approved an agreement between the Federal Government and three oil producing States to 'recover' some trillion dollars' worth of funds from largely international oil and gas companies (IOCs) allegedly due since 2003 when the price of oil exceeded $20 per barrel); and (ii) the telecoms sector (with one investor the recipient of an $8.1bn penalty for allegedly improperly repatriating funds over an eight-year period, and a $2bn retroactive tax assessment). While there is no indication that the foreign investors involved have triggered claims under BITs, these sorts of aggressive State measures are of the nature that often drive investors to launch investor-State arbitrations – or at least invoke BITs in settlement discussions. Over the next year, particularly with elections due in February, Nigeria will thus be a hot spot to watch.

> **'While many African States are increasingly adapting their political, legal and regulatory regimes to attract FDI, significant risks remain for investors in the energy and telecoms sectors in some jurisdictions – evidenced by the increasing number of Africa investor-State disputes year on year. We have significant experience working with clients looking to rely on their international treaty rights to manage such risks.'**
>
> Sylvia Noury, Partner

Nigeria also highlights another trend that we identified in last year's issue, which is an uptick in investor-State disputes, particularly in the energy and telecoms sectors, relating to taxation. Opportunistic, often retroactive and, in many cases, unlawful taxation measures are being taken by States around the world targeting foreign-controlled investments in these sectors to maximise fiscal returns – through either individual tax assessments, or general changes to their fiscal regimes, often in breach of their contractual obligations (including stabilisation measures) and treaty obligations.

A further trend in the energy sector concerns investments that are coming to their end of life, where investors are looking to hand over depleted or aging assets, and States in turn are seeking to extract final value from the departing IOCs by bringing (often unmeritorious) claims relating to operational, management, environmental and facilities issues, as well as tax and cost recovery claims. Given that a significant number of production sharing agreements (PSAs) entered into between States and IOCs in the 1980s and early 1990s are only now coming to term (or are being relinquished early given challenging economic and political factors in some areas of the world), we expect to see an uptick in the number of disputes under recently expired PSAs over the course of 2019 and beyond.



This article continues on the next page

## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 **Trends in investor-State energy and telecoms disputes: is spectrum the new oil?**

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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Moving to the telecoms sector, 'spectrum' is being increasingly viewed as a scarce resource that should be allocated in accordance with public interest principles, with maximum value extracted for the benefit of State coffers. States are thus seeking to revoke spectrum previously allocated to investors (such as the steps taken in India following the 2G spectrum scandal); seize control of foreign-owned operators entirely; or claw back some of the profits earned by investors who were allocated operating licences and spectrum years ago when their potential value was not so apparent (often through targeted tax measures, as mentioned above). We foresee an increase in the coming year and beyond in such 'spectrum value extraction' measures – reminiscent of the sorts of 'resource nationalism' measures we have seen in the energy sector over the years – and a concomitant increase in investor-State disputes.

For a more detailed look at these trends in the telecoms arbitration space, please see an article by our Associate Romilly Holland at: https://tinyurl.com/ya4325pg.

**'IOCs facing the expiry of a "PSA" with a host State should start planning a few years in advance, in order to minimise the chances of the host State initiating a time-consuming and costly post-PSA-expiry dispute. We can advise on several practical steps to take to minimise the risks.'**

Leilah Bruton, Counsel

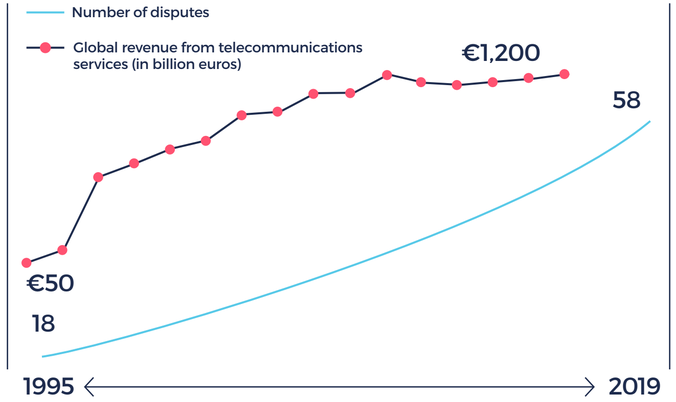
## Africa has replaced Central and South America as the dominant region for investor-State claims


14% of new ICSID cases registered in 2018 had a Middle Eastern or North African State as a party, and a further 19% had a sub-Saharan African State as a party (up from 4% of new cases in the 2017 report).


In 2018, only 12% of ICSID cases included the South American States, in contrast to over 30% in 2010.

Source: *The ICSID Caseload – Statistics* report dated June 2018
Approximately half of these cases involved the telecoms or oil, gas, mining and electricity sectors.

## The increase in the number of investor-State disputes in the telecoms sector




Source: 'Is spectrum the new oil? Trends in investor-State disputes in the telecommunications sector' by Romilly Holland, *Dispute Resolution International*, Vol 12, No 2, October 2018.

This article continues on the next page



## Contents

01 Re-designing investor-State dispute settlement
02 Trade and investment in the age of Trump
03 The future of intra-EU bilateral investment treaties following *Achmea*
04 Arbitration in the age of Brexit
05 Third-party funding: emerging norms in an ever-evolving market
06 The drive to improve efficiency in arbitral procedure: a success or more to do?
07 The impact of human rights and environmental law on investment treaty arbitration
08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?
09 Cyber security and data protection in arbitration: too important to ignore
10 The legitimacy of the arbitration process: ongoing debate and reform

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We expect an uptick in post-PSA-expiry disputes, given the number of PSAs due to expire in the next few years

| | PSAs ESTIMATED TO EXPIRE: | |
|---|---|---|
| | before 2020 | between 2020 and 2025 |
| Albania | 1 | 1 |
| Algeria | 8 | 3 |
| Angola | 39 | 7 |
| Azerbaijan Republic | 3 | 2 |
| Bahrain | 1 | 0 |
| Bangladesh | 4 | 2 |
| Brunei | 6 | 1 |
| Burma (Myanmar) | 2 | 0 |
| Cameroon | 2 | 0 |
| Chad | 1 | 1 |
| China | 20 | 9 |
| Congo Republic | 5 | 2 |
| Cuba | 1 | 0 |
| East Timor | 2 | 4 |
| East Timor/ Australia (JDA) | 2 | 0 |
| Ecuador | 0 | 2 |
| Egypt | 3 | 4 |

| | PSAs ESTIMATED TO EXPIRE: | |
|---|---|---|
| | before 2020 | between 2020 and 2025 |
| Equatorial Guinea | 2 | 0 |
| Gabon | 1 | 1 |
| Guyana | 0 | 1 |
| Hungary | 1 | 0 |
| India | 3 | 2 |
| Indonesia | 4 | 2 |
| Iraq | 9 | 2 |
| Ivory Coast | 3 | 1 |
| Jordan | 2 | 0 |
| Kazakhstan | 3 | 0 |
| Kenya | 1 | 0 |
| Liberia | 4 | 1 |
| Libya | 2 | 0 |
| Madagascar | 1 | 0 |
| Malaysia | 11 | 1 |
| Mongolia | 1 | 0 |
| Mozambique | 0 | 1 |

| | PSAs ESTIMATED TO EXPIRE: | |
|---|---|---|
| | before 2020 | between 2020 and 2025 |
| Nigeria | 12 | 4 |
| Oman | 3 | 1 |
| Qatar | 2 | 1 |
| Russia | 2 | 0 |
| Senegal | 0 | 1 |
| Sudan | 1 | 0 |
| Suriname | 2 | 0 |
| Syria | 2 | 0 |
| Tajikistan | 1 | 0 |
| Tanzania | 1 | 4 |
| Trinidad and Tobago | 6 | 3 |
| Tunisia | 1 | 0 |
| Turkmenistan | 2 | 0 |
| Uganda | 0 | 1 |
| Ukraine | 1 | 0 |
| Yemen | 2 | 0 |



## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 **Trends in investor-State energy and telecoms disputes: is spectrum the new oil?**

09 Cyber security and data protection in arbitration: too important to ignore

10 The legitimacy of the arbitration process: ongoing debate and reform



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# 09 Cyber security and data protection in arbitration: too important to ignore

The importance of cyber security grows with each passing year, and 2018 was no exception.

Nearly all major sectors in all markets experienced serious cyber security issues, ranging from hacking of customer data in India and Japan to denial of service attacks and other forms of cyber vandalism in the US. Conservative estimates suggest that there were over 100 serious cyber security breaches each month in 2018. With the proliferation of digitalisation and its extension into every facet of modern business in every corner of the world, cyber security will remain a central concern into 2019 and beyond.

Cyber security is of no less vital importance to the legal industry: clients entrust lawyers with their most sensitive information, and expect from lawyers the highest levels of care and diligence. Incidents such as the Panama Papers leak and the hacking of the Permanent Court of Arbitration, both in 2015, were a wake-up call for lawyers that still reverberates today. In any legal engagement, protection of client data has become, and will remain, a priority.

International arbitration presents a particularly difficult challenge from a cyber security and data protection perspective. In any international arbitration, highly sensitive information must be exchanged across borders by parties whose interests are not aligned. That information must also be shared with arbitrators, who may not always have the infrastructure to handle it. Other third parties, such as arbitral institutions, experts and witnesses, often will also be involved in both sending and receiving sensitive information. The result is an attractive target for those who might want to steal valuable data, or otherwise harm one of the parties to the arbitration.

The international arbitration community has begun to take encouraging steps to address these issues. In April 2018, a joint working group formed by the International Council for Commercial Arbitration, the New York City Bar Association and the International Institute for Conflict Prevention and Resolution released a draft protocol on cyber security in international arbitration for public consultation, with a view towards finalisation by 2020. In late October 2018, the International Bar Association published its own set of Cyber Security Guidelines.

Both of these documents seek to strike a balance between party autonomy and the need to promote cyber security in arbitration. Both explicitly set a goal of increasing awareness of the potential cyber security risks in international arbitration, and provide practical guidance to parties and arbitrators about how to reshape arbitral proceedings to be less vulnerable to attack.

On the data protection front, parties to an arbitration will also need to be alert to the obligations regarding transmittal of data across EU borders set out in the European General Data Protection Regulation (GDPR), which came into force in May 2018. That is particularly so given the frequent transfer of information across jurisdictions in a typical arbitration, and the lack of arbitration-specific exceptions written into GDPR.



This article continues on the next page

## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

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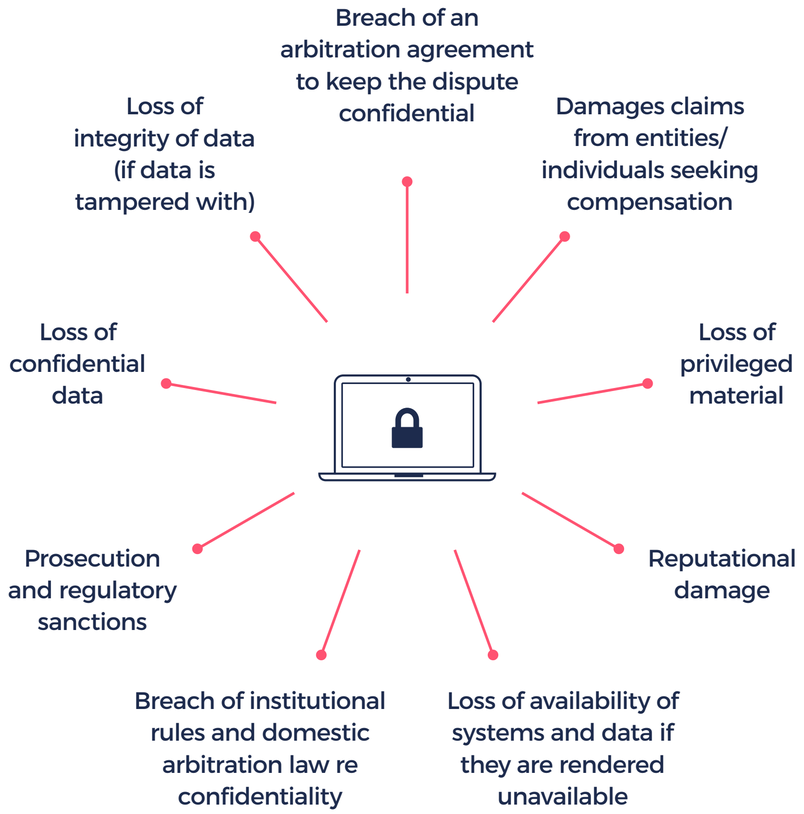
We also expect to see ancillary disputes relating to the scope of disclosure arising in connection with arbitrations, given the potential for clashes between document production orders, which may require a party to share documents containing sensitive or personal information, and European data protection obligations that may prohibit a party from doing so.

Looking to 2019 and the future, we expect cyber security and data protection issues to become increasingly central to international arbitration proceedings, and therefore increasingly contentious. Disagreement on these issues is likely to come both at the outset (eg, during procedural conferences) and in the thick of proceedings, in the form of applications for interim measures or even challenges to arbitrators. Data protection and cyber security issues should not therefore be ignored. All clients with commercially sensitive data should consider whether to minimise disagreement over these types of issues by building cyber security requirements and other technology-related points into their arbitration clauses. In either setting, the ICCA Draft Protocol and the IBA Cyber Security Guidelines provide good starting points.

**'Data protection and cyber security issues should not be ignored. All clients with commercially sensitive data should consider whether to minimise disagreement over cyber security and data storage issues between the parties to an arbitration by building technology-related points into their arbitration clauses.'**

Sami Tannous, Partner

## Risks of a cyber security attack during an arbitration






## Contents

01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

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# 10 The legitimacy of the arbitration process: ongoing debate and reform

The legitimacy of the arbitral process is fundamental to the system of international arbitration as a whole, both commercial and investment arbitration.

Arbitral tribunals have the same powers as State courts to decide disputes between individuals and/or State entities. However, their authority is conferred on them in two ways: first, the parties have to agree on arbitration to resolve disputes between them; and second, the national laws relevant for the specific dispute need to allow arbitration as a method of dispute resolution. These delegations of authority require that both the parties and the institutions involved trust the process and its legitimacy.

In recent times, the legitimacy of arbitration has been called into question. The focus as well as the merit of the issues raised in the legitimacy debate varies considerably. Examples include: how to ensure that arbitrators act diligently and improve the quality of their decision-making; whether arbitrator conflict rules are strong enough; the need to regulate and sanction counsel for unethical conduct; whether party involvement in the appointment of arbitrators ensures or lessens confidence in the arbitral tribunal; the options to increase the efficiency of the proceedings; the perceived problem that arbitral tribunals are taking too long to issue their awards; and the increasing cost of arbitration proceedings. The investor-State arbitration regime faces additional challenges of its own, in particular transparency questions and the issue of conflicting decisions on the same points of law with no single body with the authority to resolve these inconsistencies.

The arbitral community has not ignored these concerns. It has instead responded mainly with a series of reforms. Many of the main arbitral institutions have revised their rules and practices over the last few years to increase the efficiency and fairness of the arbitral process, and ICSID is in the process of updating its rules following an extensive consultation period. One notable example to address the issue of delay in rendering awards is the announcement by the ICC that it would reduce the fees paid to arbitral tribunals that fail to submit a draft award within three months of the last substantive hearing or post-hearing submission. The DIS has set similar incentives for parties and arbitrators to speed up the dispute resolution process. The perceived need to regulate counsel and party behaviour has also led to the IBA Guidelines on Party Representation in International Arbitration and the LCIA's General Guidelines for the Parties' Legal Representatives.

Demands for increased transparency have been answered in the investment realm by the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration and the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration, and in commercial arbitration by the Case Law on UNCITRAL Texts (CLOUT) project and Arbitrator Intelligence. Bilateral and multilateral investment treaties are becoming more detailed in

According to the 2018 international arbitration survey:

**80%**

of respondents would welcome rules regulating the conduct of arbitrators, including deadlines for issuing awards and consequences for delay; and

**73%**

of respondents think that the conduct of parties and their counsel should be subject to specific arbitration rules.

**'Ultimately, the flexibility of the arbitration regime – and the willingness of the arbitration institutions, practitioners and users to bring about change – should prove to be its strength.'**

Patrick Schroeder, Partner

This article continues on the next page



## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

10 **The legitimacy of the arbitration process: ongoing debate and reform**



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their provisions, often through renegotiation processes, and the debate about an appellate investment court is ever increasing.

Another aspect of legitimacy is diversity in arbitral tribunals and institutions in general. It is argued that in order to have the greatest legitimacy, tribunals should better reflect the societies and industries they serve. Gender diversity in arbitral appointments continues to make progress, driven by initiatives such as the Freshfields-founded Equal Representation in Arbitration Pledge and Arbitral Women, with the average number of female arbitrator appointments across the main arbitral institutions rising to 18 per cent for 2017 (up from around 10 per cent in 2015) with the LCIA and ICSID both reporting figures of 24 per cent. However, for other forms of diversity – including ethnic and regional diversity – similar progress is still required. Less than a third of respondents in the 2018 international arbitration survey believe that geographic, age, cultural and ethnic diversity has improved in the last five years. In 2019, we therefore anticipate further drives to increase all types of diversity in arbitration, as well as continued efforts in relation to gender diversity.

Arbitration institutions continue to increase their caseload, and the 2018 international arbitration survey reveals that for 97 per cent of the interviewees, international arbitration remains their preferred method of dispute resolution. The challenge is to foster this trend, with further effort and adaptation. Ultimately, the flexibility of the arbitration regime – and the willingness of the arbitration institutions, practitioners and users to bring about change – should prove to be its strength. In 2019 and beyond, we expect the various initiatives, rule changes and guidelines to have a positive impact. However, there will be more to do over the coming years and it is critical that drives to improve legitimacy continue. Freshfields actively participates in these processes, submitting proposals and providing comments when appropriate. Our clients are among the main users of international arbitration and we are firmly committed to improving the system to meet their needs.

**'The recent progress in gender diversity in arbitral appointments is very encouraging. But further drives to increase all forms of diversity are needed – firstly to make full use of the potential pool of talented arbitrators (which should help counter the efficiency-related criticisms of arbitration), and secondly to address the wider legitimacy concerns about whether tribunals are truly representative of the stakeholders involved in disputes.'**

Sylvia Noury, Partner
(and co-Chair of the ERA Pledge Steering Committee)

EQUAL REPRESENTATION IN ARBITRATION

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**in**

**over 110 countries**

**as at 24/1/2019**

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## Contents


01 Re-designing investor-State dispute settlement

02 Trade and investment in the age of Trump

03 The future of intra-EU bilateral investment treaties following *Achmea*

04 Arbitration in the age of Brexit

05 Third-party funding: emerging norms in an ever-evolving market

06 The drive to improve efficiency in arbitral procedure: a success or more to do?

07 The impact of human rights and environmental law on investment treaty arbitration

08 Trends in investor-State energy and telecoms disputes: is spectrum the new oil?

09 Cyber security and data protection in arbitration: too important to ignore

**10 The legitimacy of the arbitration process: ongoing debate and reform**



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