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https://doi.org/10.15017/6757914

出版情報：法政研究. 89 (3), pp.283-304, 2022-12-21. 九州大学法政学会
バージョン：
権利関係：

Japanese Investment Treaties – Reconciling Competing Interests in the Multipolar World

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INTRODUCTION

For the past many years, I have taught a course on international investment law at the University of Kyushu. During this time, I have formed a close friendship with Caslav Pejovic, who had an unrivalled knowledge of transnational and comparative business law. I have profited greatly from the many discussions I had with him both as to law and as to Japanese culture. He and his wife were generous with their time when my wife and I were in Japan and introduced us to Japanese culture and the exquisite Japanese cuisine. I take great pleasure in honouring this great scholar and friend by writing on a subject in which he and I share a common interest.

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I also write this chapter in the hope that an outsider's view of the Japanese practice may contribute to the shaping of internal policy on investment treaties. It has been a puzzle to me as to why Japan has investment treaties. They have come to be based on a gladiatorial contest when it comes to disputes and have much to do with the imposition of norms on other states. Japan does not have such a culture. Its approach is conflict avoidance. If that be so, the preferable approach would be like the one that Brazil adopted of making conflict avoidance treaties with reference to plenty of techniques of avoidance of disputes rather than make investment treaties of the Western variety. Unlike Western states whose investors have had reliance on arbitration under these treaties, Japanese investors have not had a high recourse to these treaties, until recently. The website maintained by the International Centre for the Settlement of Investment Disputes and that of the United Nations Commission on Trade and Development on investment disputes do not record many instances of Japanese entanglement with arbitration of investment disputes until recent times. In that context it is legitimate to ask why Japan should make such investment treaties. In the past, there were records of the Japanese companies being implicated in investment disputes in which larger contractors were involved but the Japanese companies did not appear as participants in the arbitration of such disputes.[1] There are however coming into being a few instances of Japanese companies being claimants against foreign states. Before answering the question as to whether Japanese treaties with strong investment arbitration provisions are relevant to Japan, particularly in the light of new developments in the subject which have eroded the significance of these treaties by diluting the investment protection aspects in them, this article first surveys the nature of the existing Japanese

(1) In *Fraport v Philippines* (ICSID Case No. ARB/03/25, 2003), an ICSID arbitration concerning the building of a second airport for Manila, a Japanese contractor was involved but did not participate in the arbitration. In *Newmont v Indonesia* (ICSID Case No ARB/14/15, 2014), a Japanese company was involved in the dispute but, again, did not appear before the arbitration tribunal. In such cases, the practice has been to let an associated company pursue the arbitration.

investment treaties, then examines the balances struck within these treaties and finally deals with the question of the need for these treaties, particularly in the context of the only case that has been brought against Japan and in the light of new trends.

1. Japanese Investment Treaties: Their Pattern

The UNCTAD International Investment Treaties Navigator lists 37 Japanese investment treaties. Of them, four have been signed but have not been ratified.[(2)] The most recent treaty is the treaty with Bahrain which was signed on 23 June 2022 but is yet to be ratified. There has been treaty activity on the part of Japan in recent times. In the last four years, treaties were signed with Bahrain, Georgia, Morocco and Cote Ivoire The fact that the practice is recent indicates that Japan would continue making investment treaties. The oldest treaty is the treaty with Egypt which was ratified on 14 January 1978. Like in the case of many states, Japan begins with weak treaties, moves into a phase of strong treaties and now makes what are known as “balanced” treaties which move away from strong protection giving the state much regulatory space. The last two treaties with Bahrain and Morocco are “balanced” treaties. It would appear that the treaties that Japan makes in the future would be broadly similar. “Balanced treaties”, as will be explained later, include the same pattern of investment protection creating liability for violation of treatment standards and expropriation provisions but contain defences in situations where measures are taken in the public interest. If that be the definition of “balanced treaties”, Japan has been making such treaties since around 2007, the year of the Japan-Cambodia investment treaty in which there are provisions that accommodate the idea that regulatory

(2) In addition, Japan is party to many regional and sectoral trade and other agreements which have investment provisions. It is party to the Energy Charter Treaty, a treaty that applies to the oil and energy sector and the Trans-Pacific Pact, a regional treaty. For contracting parties to the Energy Charter Treaty, *see* https://www.energycharter.org/process/energy-charter-treaty-1994/energy-charter-treaty/.

measures in the public interest should not be subject to liability. For the purposes of this article, the most recent treaties, those with Bahrain and Morocco are taken as the basis for discussion.

Japan is a contracting state to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States. As already stated, as at April 2022, Japan is signatory to 36 bilateral investment treaties (BITs) (of which 31 are currently in force) and 20 free trade agreements and economic partnership agreements (EPAs) that include provisions pertaining to investment protection.[(3)] Most of these instruments include investor–state dispute settlement provisions that permit investors to initiate arbitration directly against the contracting states, with the Japan–Australia EPA and the European Union (EU)–Japan EPA (mentioned below) as notable exceptions. The chapter in the Japan-Philippines FTA (2006) leaves settlement of disputes to the discretion of the parties. It envisages a future agreement on a dispute settlement provision. Australia has a policy of signing investment treaties without dispute settlement through arbitration. The European Union prefers to have disputes resolved through courts and hopes to move towards setting up a multilateral court.

Only one case has been brought to arbitration against Japan. The case, *Shift Energy v Japan*, was brought in 2020 under the Japan-Hong Kong investment treaty, 1997. Hong Kong has become a part of China but has the capacity to make its own treaties and retain treaties already made. The case involved a dispute arising from Japan's discontinuation of subsidies on solar energy. It is very similar to the situation which Spain and other European countries have faced and are facing. There are several arbitrations relating to similar measures as to solar energy which have been decided. Several are pending. The distinction may be that the measures taken by the individual European states were in reaction to policies made as to the use of alternative energy by the European Union. These

(3) UNCTAD, "Japan", *Investment Policy Hub (See* https://investmentpolicy.unctad.org/international-investment-agreements/countries/105/japan)

European states were taking measures in response to policies adopted by the regional association to which they belonged. There has been considerable secrecy surrounding the facts of the case against Japan. It is reported that the Japanese government had sought settlement of the dispute without success. Obviously, the case is seen as prejudicing Japan's reputational position as a state which has avoided foreign investment disputes.[4]

The case arose from Japan's plan to attract renewable energy projects. The European cases also arise from similar objectives. The phasing out of nuclear and other dangerous technologies in energy production in several European countries has resulted in disputes. Like the European states, Japan had also offered subsidies to attract foreign investors into the energy sector. Technology costs of solar energy decline as new and cheaper technology becomes available and more competitors enter the field. Like the European states, Japan also dismantled the originally offered concessions and tariffs affecting the expectations that the foreign investors had at the time of entry. Most of the investors who had entered the specific field were from China and Hong Kong. The *Shift Energy Arbitration* was brought by a Hong Kong company under the Japan-Hong Kong investment treaty. The Japan-Hong-Kong treaty was signed in 1997 and belongs to the period when strong investment protection treaties were signed. It is a short treaty with just 15 Articles very much in the mould of old British treaties on investment protection. It does not have the broad defences that are stated in the more recent treaties of Japan like the Japan-Morocco treaty that seek to carve out exceptions from liability for regulatory measures taken in the public interest. Though the facts of *Shift Energy* are not fully known, it would be interesting to speculate the outcome, having regard to the Spanish and other European cases. Generally, the cases already decided indicate liability on the basis of the violation

(4) *Shift Energy v. Japan* (ICSID, 2020); *See also* Leo Lewis, "Hong Kong Energy Fund Sues Japan in Groundbreaking Case" *Financial Times*, 3 March 2021 (*See* https://www.ft.com/content/155da1d7-075e-4122-adec-1e4fec51f582)

of the fair and equitable treatment provision.[5]

It is also interesting that Japanese foreign investors have been involved in the series of cases brought against European states involving solar energy. There are three such arbitrations in Japanese companies have been Claimants. One of them, *Eurus Energy Holdings Corporation and Eurus Energy Europe BV v. Kingdom of Spain*,[6] decided in favour of the Japanese claimant. The case was brought under the Energy Charter Treaty, a strong treaty in terms of investment protection, to which Japan is a party. There are three new cases brought by Japanese companies under the Energy Charter Treaty against Spain which are pending.[7] The argument will be made that Japan should continue to make investment treaties as these cases demonstrate that outgoing Japanese investments need protection.[8]

The Energy Charter Treaty has since been subjected to review with a view to modernization. It is likely that the new treaty would have a stand-alone provision that recognize the state's right to regulate, restrict the fair and equitable doctrine, considerably curtail the scope of expropriation and narrow the grounds on which jurisdiction could be claimed. From the point of view of the future, the victories in the solar energy cases may not be lasting ones. One has to take into account the changes that are taking place both in the area of investment

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（5） *Opera Fund v Spain* (ICSID Case No. ARB/15/36, 2015)

（6） *Eurus Energy Holdings Corporation and Eurus Energy Europe BV v. Kingdom of Spain* (ICSID Case No. ARB/16/4, 2016)

（7） *ITOCHU Corporation v. Kingdom of Spain* (ICSID Case No. ARB/18/25, 2018); *JGC Corporation v. Kingdom of Spain* (ICSID Case No. ARB/15/27, 2015); and *Mitsui & Co., Ltd. v. Kingdom of Spain* (ICSID Case No. ARB/20/47, 2020)

（8） Another recent case involving Nissan in India was brought to the Permanent Court of Arbitration but was settled.（*See Nissan Motor Co., Ltd. v. Republic of India*, PCA Case No. 2017-37, 2017.）A Japanese related company was involved in *Bridgestone Licensing Services, Inc and Bridgestone Americas, Inc v. Republic of Panama* (ICSID Case No. ARB/16/34, 2016). But, in *Frapport v Philippines* (ICSID Case No. ARB/03/25, 2003), an affected Japanese company preferred not to join the proceedings. So too in *Newmont v Indonesia* (ICSID Case No ARB/14/15, 2014), the Japanese company stood silent during the proceedings. There may be a preference to continue the relationship with the state despite the dispute.

treaties and in investment arbitration to assess whether the continuation of investment treaties serve any purpose for Japan given its cultural ambivalence to the adoption of gladiatorial means of dispute settlement. I shall first look at the changes taking place in investment treaties and then look at possible future trends in investment arbitration. I look at trends in international law on foreign investment before examining the question whether the making of the so-called "balanced" treaties, like the ones with Bahrain and Morocco, serve any useful purpose.

2. The Balanced Investment Treaties

There are three phases that one could identify in the making of investment treaties- a phase of weak treaties (1957-1990), a phase of strong treaties (1991-2003)[9] and a phase of balanced treaties (2004 to the present)[10]. Weak treaties resulted in no arbitrations being based on investment treaties. It was only when strong treaties came into vogue that treaty based investment arbitration took off from 1990 with the award in *AAPL v Sri Lanka*[11] announcing that an appropriately worded dispute settlement provision in an investment treaty could create a unilateral right in the foreign investor to bring claims based on treaty violations. During what I have described as the phase of strong treaties, the number of investment treaties grew exponentially exceeding over 3000 treaties and with this grew cases based on treaties which began to number over 600. In the first phase, there were only a handful of cases brought to ICSID based on investment contracts. This phase also involved expansionary interpretation of the treaty provisions extending the scope of the treaties well beyond the intention of the

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(9) This was the phase of neoliberalism and the Washington Consensus when investment treaties were driven by the untested belief that they were essential for economic development.

(10) Balanced treaties can be dated from the US Model Investment Treaty (2004, *available at* https://ustr.gov/sites/default/files/U.S.%20model%20BIT.pdf) and the Methanex Award (*See Methanex Corporation v United States*, Final Award on Jurisdiction and Merits, (2005) 44 ILM 1345.) which recognized regulatory expropriations as non-compensble.

(11) *AAPL v Sri Lanka* (ICSID Case No. ARB/87/3, 1990)

state parties which made them. New theories came to be stated by arbitrators such as the view that the fair and equitable treatment standard supported claims based on the violation of the legitimate expectations of the foreign investor at the time of entry. Likewise, expropriation law was broadened. In *Ethyl Corporation v Canada*,[(12)] for example, it was held that a ministerial statement that the banning of a chemical substance was contemplated on the ground that it was carcinogenic was held to be an expropriation as it led to the depreciation of the values of shares in the only foreign investment company manufacturing the chemical.

There was a backlash against these adventures.[(13)] They were seen as the result of a new, biased profession of arbitrators seeking to expand the law so as to create business for themselves or as the advancing of neoliberal beliefs that justified the protection of property and contract even over the need of a state to act in the public interest. The result was that states began to reconsider the treaties made in the second phase that emphasised investment protection without considering other factors such as the state's need to protect the public interest.

The decision in *Methanex v US*[(14)] was an important award that signalled the change. It, like Ethyl, involved the manufacture of a carcinogenic substance by a foreign investor. Its use was banned. The United States successfully argued that there was no expropriation that was compensable as the state had acted in order to protect the public health. In the context of this award and the manner the United States argued the case, there was a revival of the rule relating to regulatory expropriation that when in pursuance of its police powers a stated acted in the public interest, the harm that is caused by the measure should not be regarded as a compensable expropriation. The rule came to be stated in the investment treaties of the United States. The 2004 Model Investment Treaty of

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(12) *See* its Award on Jurisdiction dated 24 June 1998 (UNCITRAL). Canada settled by paying some 13 million dollars as damages after the jurisdiction phase.

(13) Michael Waibel et al. (Eds.), *The Backlash against Investment Arbitration* (Kluwer, London, 2010)

(14) *Methanex Corporation v United States of America* (ICSID, 1999)

the United States contained the rule. 2004 may safely be taken as the time when the "balanced" treaties which supposedly balanced the emphasis on investment protection with the regulatory interest of the state began. The Model Treaty also began the practice of stating possible defences to liability which the state could plead, such as that the measure was taken to prevent environmental harm. In the earlier treaties such defences are not stated with much force but later treaties contain strong statements of these defences. The distinction between the 2004 US Model Treaty and the 2012 US Model Treaty is based largely on the defences being stated more assertively in the later treaty.

Japan also has begun a practice of "balanced" treaties. Its treaty with Cambodia (2007) contains carve out for financial services and taxation and has defences. It is interesting that one of its recent treaties is with Morocco (2020). Morocco had signed a treaty with Nigeria in 2016 which was regarded as an innovative treaty containing a fine balance between protection of investment and the regulatory power of the state.(15) The Japan-Morocco treaty matches the innovating Nigeria-Morocco treaty and for that reason, its main features deserve being noted.

The preamble of the Japan-Morocco Treaty states the regulatory interest of the state at the outset of the treaty. It states in the preambular provision that the treaty "recognises the inherent right of the Contracting Parties to regulate and to preserve their flexibility to set legislative and regulatory priorities, safeguard public welfare, and protect legitimate public welfare objectives, such as public health, safety, the environment, the conservation of living or non-living exhaustible natural resources, the ~ integrity and stability of the financial system and public morals". The Nigeria-Morocco treaty does not state this regulatory

(15) Okechukwu Ejims, "The 2016 Morocco–Nigeria Bilateral Investment Treaty: More Practical Reality in Providing a Balanced Investment Treaty?", 34(1) *ICSID Review - Foreign Investment Law Journal* 62 (2019); and Tarcisio Gazzini, "The 2016 Morocco–Nigeria BIT: An Important Contribution to the Reform of Investment Treaties", *Investment Treaty News*, 26 September 2017 (*See*, https://www.iisd.org/itn/en/2017/09/26/the-2016-morocco-nigeria-bit-an-important-contribution-to-the-reform-of-investment-treaties-tarcisio-gazzini/)

power in such exhaustive terms. The statment is contained in its preamble, though it states the regulatory power of the state in a later section of the treaty in wide terms. The Nigeria-Morocco treaty also states defences to liability in broad terms. It deals with corporate social responsibility and corruption. It contains an interpretive commission that could make authoritative statements regarding provisions of the treaty. These innovations are missing from the Japan-Morocco treaty. Nevertheless, the Japan-Morocco treaty as well as the Japan-Bahrain treaty show that Japan has embraced balanced treaties.

The so-called "balanced" treaties are not very sound in theory. The idea that investment protection can be balanced with the state's obligation to protect the public interest itself involves an incompatibility. A state's obligation to further the public interest is more paramount than any other consideration including the protection of the foreign investor. Put in terms of a balance, the idea involves a constitutionally unacceptable notion. Since the safety of the people is always the paramount consideration for the existence of a state, the idea that it can be balanced against the interest of a foreign investor seems to be unsound in terms of constitutional theory. Besides, in the context of its paramountcy, the notion of the regulatory power of the state cannot be relegated to the position of defences after liability is found. The exercise of such power excludes all liability.

Whatever the theoretical criticisms are, the practical effect of such treaties are also doubtful. Ultimately, the treaties have to be interpreted by arbitrators who as a class of persons would be loath to interpret the regulatory power of the state widely as it would not give too much leeway for the holding of liability. The effecting of a true balance would be a difficult task. The subjectivities of arbitrators will take over in the performance of such an exercise. The balanced treaty invites the reconciliation of mutually incompatible objectives, the protection of foreign investment and the state's objective of promoting the public interest. Except on the spurious argument that the objectives are compatible because foreign investment promotes economic development, which

is no longer taken seriously, the incompatibility of public interest objectives like the prevention of environmental depletion, the promotion of human rights, the elimination of corruption, the enhancement of corporate social responsibility, the protection of indigenous communities, the preservation of cultural property and the safeguarding of labour rights which are increasingly referred to in balanced treaties as foundation of defences are increasingly evident. A reconciliation of conflicts in this area calls for an objectivity which cannot be expected from the present practititoners of arbitration who have been groomed in an inflexible belief that foreign investment must be protected as an absolute rule.

One can find this reluctance in the first case involving a balanced treaty-*Eco Oro Ltd v Columbia.*(16) It involved a situation of a foreign investor given a concession for a mining project in the Colombian paramos, a mountain stretch of nature in which indigenous communities lived. This mountainous ecosystem provided significant biodiversity. It contained aquifers which supplied water to many communities. The disturbance of the area would contribute to climate change. The Canada-Columbia FTA was drafted so as to take care of such considerations. It is a balanced treaty in that it makes regulatory expropriations non-compensable(17) and excludes liability for non-discriminatory environmental measures.(18) The tribunal in *Eco-Oro* dismissed the claim on expropriation on the ground that it was a regulatory taking inspired by the need to protect the environment but upheld the claim that there was a violation of the fair and

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(16) *Eco Oro Minerals Corp. v Republic of Colombia* (ICSID Case No. ARB/16/41, 2016)

(17) Annex 811(2)(b) of the Canada-Colombia FTA: "Except in rare circumstances, such as when a measure or series of measures is so severe in the light of its purpose that it cannot be reasonably viewed as having been adopted in good faith, non- discriminatory measures by a Party that are designed and applied to protect legitimate public welfare objectives, for example ... the protection of the environment, do not constitute indirect expropriation."

(18) Article 2201(3) of the Canada-Colombia FTA: "For the purposes of Chapter Eight (Investment), subject to the requirement that such measures are not applied in a manner that constitute arbitrary or unjustifiable discrimination between investment or between investors, or a disguised restriction on international trade or investment, nothing in this Agreement shall be construed to prevent a Party from adopting or enforcing measures necessary: ... (c) For the conservation of living or non-living exhaustible natural resources."

equitable standard of treatment despite the fact that the treaty itself states that this standard is not different from the minimum standard treatment of customary international law. The fault is that the fair and equitable standard was stated in the treaty despite the statement that it was no different from customary international law. If so, it should have been simply left out. It is difficult to understand the formula in North American treaties which include the fair and equitable treatment and state that it is not different from the customary law on the international minimum standard. The reluctance to exclude the fair and equitable treatment provision is unexplainable except on the secret desire that it should continue to be used in an expansionary manner as the *Eco-Oro* tribunal did. This explanation requires belief in the insensitivity of the draftsmen.

On the basis of the inclusion of the fair and equitable treatment, the tribunal in its majority award held that the legitimate expectations of the foreign investor at the time of entry had been violated. The law is that the regulatory powers doctrine would apply to the violation of the fair and equitable standard as well. The tribunal, as the partial dissent points out, was making an error in the use of the legitimate expectations interpretation which in itself is an expansion that arbitrators had earlier made of the provision on fair and equitable treatment.

The Eco-Oro award demonstrates that the new "balanced" treaties will not succeed in their purpose of restraining the adventurousness of arbitrators in enhancing foreign investment protection to the regulatory interests of the state. Indeed, what makes the Eco-Oro Award obnoxious is that Columbia was advancing a global interest in protecting the environment from climate change in its prohibition of mining in the Columbian paramos. The fault lies with the system rather than in how treaties are drafted. The treaties are embedded in a system of dispute resolution wedded in the outdated theory of economic development supported by the World Bank. It has acquired a baggage of old school commercial arbitrators believing in the sanctity of the contract and carpet-baggers in the legal profession and large law firms who want to milk the cash

cow of investment arbitration through outlandish theories of litigation. If the so-called balance in the new treaties is to have any chance of success, there must be a systemic change locating settlement of investment disputes within a fresh set-up that ensures that the existing system of arbitration and its carpetbaggers do not feature in it. Japan should make a careful response in fashioning its treaty practice in the light of these events as well other developments in international law that are detailed below.

3. International Law and Its Changes

The changes that are taking place within the international law in foreign investment will ensure new attitudes to the settlement of investment disputes. In the neoliberal period of strong theories, the law was subverted by mercenary international lawyers and arbitrators to serve the instrumental purpose of furthering the interests of multinational corporations through the adoption of an unproven theory that foreign investment protection through treaties promoted economic development.(19) The legitimacy crisis that followed the adventurous expansion of the standards of protection of foreign investment through arbitral awards resulted in various responses from states. South Africa withdrew from treaties, making its domestic law the solely applicable law to foreign investments and the domestic courts the sole arbiters of disputes with foreign investors. Some Latin American- Uruguay, Ecuador and Venezuela- states withdrew from international arbitration systems. Some states terminated their existing treaties. The newer type of treaties that they replaced them with have narrow grounds on which liability can be found. Most other states have replaced their old treaties with “balanced” treaties. Japan falls into the latter category, though it did not terminate its old treaties.

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(19) The theory has been subjected to doubt in economic literature. *See, for example,* Lauge Poulsen, *Bounded Rationality and Economic Diplomacy: The Politics of Investment Treaties in Developing Countries* (Cambridge University Press, 2015).

But, the most important development has been the return of the subject into the fold of public international law from within which it had its origins. With the advent of the strong treaties and neoliberalism, the subject was hived out from its moorings and developed as a distinct subject in a silo by an epistemic community which was not steeped in public international law. The instrumental development of the subject was devoted to the promotion and protection of foreign investment, the protection of contracts and the preservation of property which were goals of the prevailing neoliberal economic philosophy. This fundamentalist philosophy has become dented and those who supported it are now discredited. This has facilitated the return of the subject of foreign investment to its fold within international law.

The return to international law coincided with the end of fragmentation of international law. Hitherto, international law had been developed in compartments as it suited the hegemonic interests which were able to give expression to its instrumental designs within the demarcated compartments without heeding other areas and principles of international law that may impact on these separate compartments. That project crumbled as increasing demands were made to test every area in the context of general principles of international law and in the context of compatibility with rules in other areas of international law. The international law on foreign investment had to adhere to this change that was occurring. The change presaged a major restructuring of the international law on foreign investment which is now ongoing. Its impact is assessed in the paragraphs that follow.

First, one must start with the injunction in the Vienna Convention on the Law of Treaties which demands that treaties be read in the light of principles of international law. Bilateral and other investment treaties cannot be exceptions to this rule. Whole range of international principles become relevant to the interpretation of treaties. They must be factored into the investment treaties even if not expressly stated as states can make treaties only within international

law and they must be taken as having consented to doing so. Where the treaty does not expressly mention a principle, it must be inferred. Take, for example, a principle like national security as a preclusion to liability. It is sometimes not stated in investment treaties. In such treaties, it must be inferred as national security is an attribute of state sovereignty under international law. Where it is stated, and there is a deficiency in its statement, the deficiency must be made up by international law which may recognize a broader doctrine of national security than the one stated in the treaty.

The one area of public international law that is most relevant to foreign investment is the area of state responsibility. There is a draft code on this subject by the International Law Commission. It has remained a draft code because it has not received the support of a large number of developing countries. These states believe that the draft code contains statement of principles in a manner that is inimical to the interests of developing states. Yet, the practice within investment arbitration has been to treat this code and its principles as if they were binding. Many awards have been made on this false assumption. The rule on necessity provides an example where it is stated that necessity will not provide a defence if there is an alternative that is less onerous to the investor. There is no authority in customary international law for the statement of the defence of necessity in this restrictive manner. It would be invidious to expect a state faced with a state of necessity that imperils its citizens to think of the comforts of the foreign investor. In *CMS v Argentina*,[(20)] the rule in the draft code was inflexibly applied in holding that the devaluation of the Argentine peso which caused an adverse effect on investors was not covered by necessity as there was the alternative of meeting the economic crisis by securing a loan from the International Monetary Fund. There is no record to show that this is a meaningful alternative. In any event, in the midst of a crisis, the state's appreciation of the events and

(20) *CMS Gas Transmission Company v The Argentine Republic* (ICSID Case No. ARB/01/8, 2001)

solutions to it should surely be given preference to what three arbitrators who are not experts in economic crises decide afterwards in the cool comfort of the arbitration hearing room.

Other defences and other principles of international law become similarly relevant when it comes to the application of investment treaties. There will be a progressive interpretation of liability under investment treaties in the light of principles of public international law. This would change the substantive rules of the subject significantly. One has to judge the future relevance of investment treaties in the light of the relevance of these developments. I attempt a prediction of the future course of events in the next section.

4. The Future Course of the Law

The law on investment protection is at the crossroads. States have a decision to make as to whether the existing law based on investment treaties is the solution to the problem. The excesses of the system that was worked out has made the states which devised the system look askance at it. Besides these once hegemonic states have seen their power being drained. They had formulated these principles at a time when they had uncontested power. The United States, the leader of the unipolar world during the period when there were strong laws on investment protection, itself desires changes to the law. Not only has it espoused balanced treaties but it has initiated and embraced the idea of regulatory powers and their primacy when public interests demand such a course.

Besides, in the emerging multipolar world, with the resurgence of China and India and other states like even Singapore becoming exporters of capital, the United States has now become the largest capital importing state. Its interests as well as the interests of its European allies have undergone significant changes. They are now seeking to conserve their territorial sovereignty over foreign investment that enter their states. They are especially intent of countering the growing technological strength of China.

The use of the national security will become more significant as time advances. The formation of a Western alliance against China will ensure that Chinese technology companies will not have easy access into the markets of the United States and its European allies. The use of national security exclusions in investment treaties will become frequent as a means of excluding Chinese investments. The Huawei incidents in the US and Canada presage these trends. Despite the existence of investment treaties, there will be increasing efforts made to keep Chinese investments out. Likewise, in the areas of patents and intellectual property, the need for compulsory licensing of drugs in times of pandemics will undermine the protection of the pharmaceutical industries through investment treaties.(21) The national security plea covers patent infringements in times of pandemics as pandemics cause serious threats to the lives of people as great as war. Even without treaty statements of the defence, the defence could be invoked on the basis of general international law.(22) Whereas national security was thought of as embracing military matters, in modern law it extends into other spheres like diseases, technological secrets, access to information about citizens,(23) the running of media, services involving political propaganda and similar areas. The broadening scope of the national security defence makes investment protection tenuous.

There are other areas of general public international law which will weaken the protection given by investment treaties. The rule that the ius cogens principles oust inconsistent treaty obligations would mean that investment treaties could not give protection to investment that violate these principles.(24) Thus, for example, an investment that employs slave labour or conduces to

(21) The reverse engineering of patented drugs and parallel importing became common during the spread of AIDS. The Doha Declaration amended TRIPS by permitting parallel importing. The Covid pandemic also weakens the case for patent protection of drugs.

(22) India invoked the defence with partial success in *Devas Ltd. v India* (PCA Case No. 2013-09, 2012) though there was no military threat.

(23) This is indicated in concern with Tik Tok and other digital platforms run especially by Chinese companies.

(24) Article 51 of the Vienna Convention on the Law of Treaties excludes treaty obligations inconsistent with ius cogens obligations.

genocide cannot claim the protection of investment treaties.[25] One could anticipate that there will be efforts to expand the rule into areas such as rules against climate change or the protection of indigenous people.

Along similar lines, it can be argued that the growing tendency within international law to protect the environment, human rights, cultural property and labour standards will general arguments that these concerns reflect those of the global community and must be given superior ranking within a system of obligations to investment protection which serves only the interests of multinational corporations and elite groups which support them. Many of these factors are mentioned as defences to liability in the new "balanced" treaties. But, a stronger case can be made in the general international law on the basis that these are growing areas of multilateral concern and that in the hierarchy of obligations within international law they stand higher than the obligations created by bilateral investment treaties or even regional investment treaties. The developments that take place in these areas progressively weakened.

The most important of these developments will be in the area of climate change. The world is facing a common challenge of forestalling a major calamity. The measures that are taken to control climate change are most likely to affect foreign investment made by multinational corporations. Eco-Oro v Columbia gave an example of possible future conflicts that could arise. In such circumstances, the measures taken to protect against climate change must trump those involving investment protection for the obvious reason that global interests of great significance motivate those measure which should not be impeded by the obligation to protect the interests of investment protection. *Eco-Oro* indicates opposition to this idea particularly by those prone to mercenary objectives of advancing the preservation of investment arbitration. But, sense requires that such narrow interests be subjugated to the global interest of preventing

(25) *Desert Lines v Yemen* (ICSID Case No. ARB/05/17, 2005)

climate change. In *Eco-Oro*, the Columbian courts had made a far more sensitive assessment of the conflict between the foreign investment and the climate change objectives than the tribunal. The tribunal, which consisted of three persons, with no appreciation of the local circumstances sought to interfere with the judgments of the local courts which they cited in detail and which contained more sophisticated analysis of the situation than the tribunal's award.

There are other factors related to public international law which are appearing in treaties. They undermine the relevance of treaties. Three such factors may be identified. There are carve out of two sectors, matters affecting prudential affairs and taxation. The third is the inclusion of an interpretation commission consisting of appointees the state parties that makes an interpretation by the commission binding on the arbitration tribunal, thus preventing adventurous, expansive interpretation by the parties. Each of these three factors deserve examination.

The carving out of the prudential sector is relevant in the light of measures taken during economic crises. These measures have an effect on investments. The several arbitrations brought against Argentina arose out of measures taken during an economic crisis.[26] The awards were made before the rediscovery of regulatory expropriations in *Methanex*. Clearly, there was room for the argument that these measures were regulatory in nature and were a response to the public interests affected by the crisis. In the later Greek case, such a defence was successfully pleaded. The belief that the global economic crisis of 2008 would result in a glut of cases did not eventuate because of the fact that the measures taken in response to it in the various countries would certainly have been held to be regulatory.

The facts in *Rafat Ali v Indonesia* were different.[27] Here, the Central Bank of Indonesia sought to reorganize the banking system by requiring that the smaller banks merge so that they could form large banks with more capital assets so

(26) Fifty-two arbitrations were brought against Argentina. The cases abated after two tribunals found that the plea of necessity covered the situation. *See LG&E v Argentina* (ICSID Case No. ARB/02/1, 2002) and *El-Paso v Argentina* (ICSID Case No. ARB/03/15, 2003).

(27) *Rafat Ali Rizvi v Republic of Indonesia* (ICSID Case No. ARB/11/13, 2013)

that possibility of an economic crisis could be averted. The separate opinion in that case held that the measure taken by Indonesia was a prudential measure in anticipation of economic crisis and should not be subject to arbitration.[28] Indonesia has since then carved out the prudential sector from the jurisdiction of arbitration tribunals in its investment treaties.[29] Article 20 of the Japan-Bahrain treaty contains an ambivalent effort that is made to carve out the prudential sector, there being a conflict between the provisions of the two sub-articles.[30] But, the Article does indicate the desire of the parties to carve out prudential measures. This means that an important area in which cases had arisen in the past will be excluded in many modern "balanced" treaties.

A similar carve out is made for taxation in modern treaties. In the older cases, the issue whether taxation was expropriation had been considered. Taxation is quintessentially sovereign act of a state. Modern treaties carve out taxation for separate treatment. Some boldly state that taxation is not an issue to be considered by an arbitration tribunal. Some require it to be considered by a joint committee and permit the matter to be submitted to arbitration only if the committee approves. Again, this idea appears in the recent Japanese treaties.[31] An important area of disputes is carved out of the treaty.

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(28) M. Sornarajah, "Separate Concurring Opinion of Professor Muthucumaraswamy Sornarajah", *ICSID Award on Jurisdiction in Rafat Ali Rizvi* (16 July 2013)

(29) *See* Singapore-Indonesia Bilateral Investment Treaty (2022).

(30) Article 20 of the Japan-Bahrain Treaty (Prudential Measures): "1. Notwithstanding any other provisions of this Agreement, a Contracting Party shall not be prevented from taking measures relating to financial services for prudential reasons, including measures for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by an enterprise supplying financial services, or to ensure the integrity and stability of its financial system. 2. Where the measures taken by a Contracting Party pursuant to paragraph 1 do not conform with this Agreement, they shall not be used as a means of avoiding the obligations of the Contracting Party under this Agreement."

(31) *See, for example,* Article 18 of the Japan-Morocco Treaty (Taxation): "1. Nothing in this Agreement shall affect the rights and obligations of either Contracting Patty under tax convention. In the event of any inconsistency between this Agreement and any such convention, that convention shall prevail to the extent of the inconsistency. 2. An arbitral tribunal established under Article 16 shall not have the authority for interpretation or application of the tax laws of either Contracting Party."

There are provisions in newer treaties which establish joint committees of the parties to interpret provisions of the investment treaties. The interpretation would be binding on the arbitral tribunals that consider provisions involving disputes prior to or during the proceedings. The conclusiveness of the interpretation ensures that the arbitral tribunal has no further say on the subject. Again, the role of the arbitration tribunal is limited.

What we see happening now is the emergence of many factors both within treaties and in the public international law within the context of which the treaties have to operate constricting the function of investment protection which had been the rationale for the making of investment treaties. That rationale has become increasingly obsolete. This erosion of the ability of investment treaties to offer protection to foreign investors removes the justification for the existence of the treaties. The only justification that states like Japan have for making investment treaties are that outgoing investments receive protection through them. That rationale no longer exists as the "balanced" treaties hem in the protection function through broad defences and care out many areas from its scope. Besides, developments in public international law do not appear to be congenial for the retention of the investment protection function of investment treaties. Multilateral treaties like the Energy Charter Treaty, the basis of many investment cases that are pending, including the *Hulley Case* against Japan will undergo similar changes and become "balanced" treaties. It is best for each state to start rethinking the usefulness of investment treaties.

States are beginning to rely more on domestic laws to deal with foreign investment. South Africa is the obvious model of a state adopting a foreign investment law as the sole arbiter of all matters relating to foreign investment. China's 2020 Foreign Investment Law seems to be a comprehensive document that makes its local courts and tribunals the arbiters of foreign investment issues though there is room left for international arbitration if the domestic courts deny justice. The foreign investor who enters China must be taken as agreeing to the

system in the domestic law.

CONCLUSION

In view of the changes that are taking place in the area, Japan and other states should rethink the relevance of investment treaties and their content. The system of dispute settlement under them has resulted in much adverse criticism. The idea of a multilateral court is not an answer as there is no guarantee that many of the defects will not be repeated by such a court. The better system may be to return to the old law where remedies were provided by the domestic courts of host states and, where such courts deny justice, the home state interferes to protect the investment through diplomatic means or through litigation before available international courts. Some investment treaties, like the Indian model treaty, are already inclining towards such a situation by confining their remedies to situations where there is a denial of a remedy.