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# EU-Singapore Investment Protection Agreement

## Legal analysis

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The Commission intends to pursue a trade policy ‘based on values’.[1] The EU Treaties make clear that this is not only a policy preference but also a legal obligation. The Treaties state that in its relations with the wider world, the EU ‘shall uphold and promote its values’, ‘contribute to the sustainable development of the earth’ and the ‘eradication of poverty and the protection of human rights, in particular the rights of the child’.[2] Moreover, the ‘Union's action on the international scene shall be guided by [...] democracy, the rule of law, the universality and indivisibility of human rights and fundamental freedoms’.[3] In light of these policy objectives and legal guidance, the EU should not promote International Investment Agreements (IIAs) that would allow investors to bring claims that violate these values.

Despite minor improvements, the EU-Singapore Investment Protection Agreement (EUSIPA) fails to safeguard human rights, democracy and the rule of law, both in Europe and Singapore. The present legal analysis reveals that EUSIPA does not fundamentally depart from the old generation of Bilateral Investment Treaties (BITs), as regards both procedural and substantive aspects.

Key findings

- **Right to regulate without effective public-interest carve-out**
  The right to regulate is reaffirmed, but the formulation is declarative and not legally enforceable. There is no proper carve-out to effectively limit claims that challenge public policy measures. There is no supremacy clause clarifying to Tribunal members that investment protections do not outweigh the EU’s obligations arising out of international environmental, social and human rights agreements.
- **Erosion of policy space by vague and unqualified standards of protection for investors**
  The agreement contain wide and outdated investors protection standards, such as the fair and equitable treatment standard (FET) and indirect expropriation. The agreement codifies the ‘frustration’ of ‘legitimate expectations’ of an investor, one of the most far-reaching interpretations of the FET and include an explicit “umbrella” clause which allows any contract from a State entity, at any level, to be directly challenged before an international investment court rather than domestic courts.
- **No limit to the amount of compensation**
  The agreement fails to clarify that ‘the loss suffered by the investor’, which will have to be compensated for, does not include expected profits based a speculative assessments of future value of the company. Awards should be limited to cover only the value of proven economic damages resulting from the breach of the agreement.
- **Broad definition of covered investor and investment**
  The agreement fails to define investor/investment in a way that would only allow responsible investors to bring claims.
- **Failure to address the key flaws of ISDS**
  The ICS only enhances the consistency and the predictability of the system. It remains a biased parallel judicial system for investors to sue states, which does not respect the powers of the domestic courts and the autonomy of the EU legal order. Moreover, there is no sufficient guarantee of judicial independence of Tribunal members who decide on cases from a narrow trade/investment perspective, without sufficient knowledge of domestic law or expertise in public policy fields.

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[1] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Trade for All Towards a more responsible trade and investment policy, COM/2015/0497 final

[2] Article 3 (5) TEU

[3] Article 21 (1) TEU

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## 1. Procedural issues: dispute settlement

While the EU has understood the need to reform the investor-state dispute settlement (ISDS), the reforms have not addressed the key flaws of the system. The Investment Court System (ICS) included in CETA[4] and which is also part of the EUSIPA, only enhances the consistency and the predictability of the system, but does not constitute a progressive approach.

### 1.1. Respect for domestic courts and the EU legal order

Article 3.13 (applicable law) of EUSIPA seeks to accommodate one of the key constitutional flaws of ISDS under EU law: its incompatibility with the EU Treaties. The article seeks to preserve the powers of the European Court of Justice (ECJ) and the autonomy of the EU legal system by limiting the powers of the Tribunals in relation to domestic law. However, these precautions are not sufficient to take into account the fundamental concerns regarding the compatibility of the agreement with the EU Treaties.[5]

The agreement **does not oblige parties to the proceedings to exhaust local remedies** (ELR) before bringing a claim at the international level. The ELR is an important rule of international law that gives the State where the violations occurred an opportunity to redress it by its own means, within the legal framework of its domestic legal system. EUSIPA therefore goes against a standing practice in international law and perpetuates the privileged status of foreign investors under international investment law.[6] Both Singapore and the EU have advanced legal systems, based on the rule of law, which guarantee adequate judicial protection for foreign investors and there is no evidence of systematic discrimination of foreign investors in either jurisdiction. Article 3.7 (conditions to submit claims) of EUSIPA only requires investors to choose between going to national (or international) courts or the investment arbitration mechanism under the agreement. The provision intends to avoid parallel claims by requiring to withdraw existing procedures in a domestic court or under another BIT and to waive the right to initiate a claim in these fora with respect to the same measure (fork in the road principle).

Moreover, the agreement **does not require the ICS to involve domestic courts or authorities** of the host State for matters of domestic law.[7] As explained in the next section, investment arbitrators are generally specialists in international investment law, and are not necessarily familiar with the intricacies of a domestic legal system. Only by requiring them to defer to local authorities can it be assured that they do not incorrectly read or apply domestic rules, or subordinate unfamiliar social and environmental interests to familiar investment ones.

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[4] As a reminder, the European Court of Justice is currently deciding on the legality of the ICS under CETA in *Opinion 1/17*.

[5] Laurens Ankersmit and Karla Hill, "Legality of Investor-state dispute settlement under EU Law" (ClientEarth Legal Study 2015), https://www.documents.clientearth.org/wp-content/uploads/library/2015-10-15-legality-of-isds-under-eu-law-ce-en.pdf

[6] There are a few IIAs that do explicitly require ELR, including those of several Member States. See for instance the recent Albania-Lithuania Bilateral Investment Treaty and the Romania-Sri Lanka Bilateral Investment Treaty. An ELR clause could also be formulated as follows: "A state party, an investor, or an affected third party must exhaust local administrative and judicial remedies before it may submit a claim before the arbitration tribunal seeking damages for an alleged breach of an International Investment Agreement."

[7] Inspiration for this requirement to refer can be taken from the draft agreement providing for the accession of the European Union to the Convention for the Protection of Human Rights and Fundamental Freedoms

## 1.2. Independence and impartiality of Tribunal members

Articles 3.9 to 3.11 of EUSIPA seek to address another of the core criticisms of ISDS - the lack of independence and bias towards investors of ISDS arbitrators - by modifying the selection process of Tribunal members. Tribunal members will be randomly selected from a roster of six individuals, appointed for eight years by a "Committee". While the selection process is a step in the right direction, it still does **not guarantee sufficient judicial independence**:

- Tribunal members are (still) not financially independent. They receive a monthly retainer fee, but are still paid for the amount of work they carry out, creating a financial incentive to hear cases in a one-sided system in which only investors can bring claims. Moreover, Tribunal members may still work as ISDS arbitrators in other cases brought under the old system.[8]
- The selection process of the roster of Tribunal Members by the Committee is opaque and lacks objective criteria and concrete rules on appointments or scrutiny by the public or their democratically elected representatives.
- This system opens the interpretation of complex, sovereign public policy decisions up to Tribunal members who will evaluate them from a narrow trade/investment perspective with insufficient knowledge of domestic law or expertise in public policy fields.

Furthermore, according to Article 4.1 of EUSIPA, the Committee has several important powers, but there are no rules which determine how the Committee can be publically held accountable for its decisions, nor are there any clear rules on its composition, decision-making, and transparency. It not only appoints the roster of Tribunal members, but it can also adopt definitions of the 'fair and equitable treatment' standard and adopt interpretations of provisions in the investment chapter that will be binding on Tribunals, even while a case is ongoing. These factors contribute to making ICS unpredictable and potential prey to influences seeking to undermine public interest decision-making processes. The powers of the Committee are problematic because it can change features of the agreement without democratic oversight or accountability and undermine the power of courts to interpret EU law.

It remains thus to be seen in practice how this new court system will avoid replicating the old system. Indeed, one may question how ICS ensures that the members of the Tribunal are not selected from the inner circle of investment lawyers that have until now driven the boom of the arbitration industry. Nothing in the agreement ensures diversity of arbitrators, nor requires a wider set of competences and qualifications. Moreover, the commitment to sustainable development that the Parties reaffirmed in the Preamble is meaningless if competence and expertise in human rights and environmental law are not part of the qualifications of arbitrators.

## 2. Substantive issues: investment protection

Besides the procedural issues, the agreement does not either challenge the outdated formulations of investment regulation, nor embrace substantive changes to preserve regulatory space and

[8] Article 3.11 (Ethics) states that "In addition, upon appointment, they shall refrain from acting as counsel, party-appointed expert or party-appointed witness in any pending or new investment protection dispute under this or any other agreement or domestic law." The only obstacle seems to be the conflict of interest rules referred to under Article 3.11 and Annex 7 (Code of Conduct) that regulates the issue of Independence and Impartiality, but they are much too weak and do not prevent Tribunal members to work as ISDS arbitrators

reorient priorities towards broader sustainable development objectives. Greater consideration should thus be given to the implications of substantive provisions contained in the agreement, i.e. whether they ensure that the agreement (1) does not undermine the ability of European Member States to regulate in the public interest and (2) can be used only by responsible investors.

## 2.1. Right to regulate

It should be born in mind that the parties, by definition as sovereign entities, possess the right to regulate. Article 2.2 of EUSIPA is intended to strengthen such right and is thus welcome. The purpose of its inclusion is to define the balance between the sovereign right of a party to regulate in the public interest and its obligations towards foreign investors. However, the first paragraph merely 'reaffirms' the already existing balance. The following paragraph offers some improvement, but it cannot properly be construed as a carve-out for decision-making in the public interest. The formulation of this article is declarative and not legally enforceable. It is merely a guideline for arbitrators.

This provision therefore **fails to effectively limit claims that challenge public policy measures**. This clause does not secure the right to regulate as wordings designed to exclude public interest measures from the scope of investment protection do not necessarily prevent investors from suing and arbitrators are not likely to discard a case due to such an exception clause.

The inclusion of a proper public interest carve-out would ensure that investors cannot challenge legitimate public interest regulations in the first place.[9] Such a carve-out is extremely important because one of the most serious criticisms of ISDS as it currently exists is that investors have used it to challenge national environmental, health, and human rights rules, or to pressure States not to adopt such rules under threat of litigation. In other words, under EUSIPA a government may adopt public interest regulations, but will still be required to pay millions in compensation to investors if those regulations infringe their rights.

Furthermore, the agreement does not contain a supremacy clause clarifying to investment arbitrators that investment protections do not outweigh the EU's obligations arising out of international environmental, social and human rights agreements.[10] In the event of a conflict between these rules, investor protections would prevail over public social and environmental obligations. Countries must have the policy space they require to fulfil their international social and environmental commitments, such as the Paris Agreement on climate change. Such a clause would address the current issue in a number of ISDS cases, where investment arbitrators have found that obligations under international environmental or human rights agreements cannot justify infringing on investors' rights.

[9] A carve-out to protect public policy measures could be formulated as follows: "Any measure or action undertaken by a Party that aims or has the effect of contributing to a public interest, such as environmental protection including measures or actions combating climate change, social protection, consumer protection, and public health protection, does not constitute a breach of the provisions of this Chapter." Another example can be found under the Nigeria-Morocco Reciprocal Investment Promotion and Protection Agreement, 3 December 2006, Article 23.3, https://investmentpolicyhub.unctad.org/Download/TreatyFile/5409

[10] A supremacy clause could be formulated as follows: ""In the event of any inconsistency between an international investment agreement and any international environmental, social, or human rights agreement binding on one Parties to a dispute, the obligations under the international environmental, social, or human rights agreement shall prevail."

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## 2.2. Investment protection standards

The EU did not walk away from the most controversial old IIAs features, and included vague and unqualified standards of protection under Articles 2.3 to 2.5 of EUSIPA. Nothing in these provisions effectively protects policy space from erosion by investment protection standards.

- Fair and Equitable Treatment

Article 2.4 of EUSIPA accords Fair and Equitable Treatment (FET) to investors and investments, which has become the centrepiece of most modern investor claims. This protection imposes a general obligation on the host State to provide a stable investment environment in which the investor's reasonable expectations should not be violated. Known as **"catch-all" provision**, it has allowed investors to challenge public policy measures through arbitration and has been interpreted in an inconsistent and far-reaching manner that can result in expansive obligations imposing a high threshold of protection in favour of the investor.

Article 2.4 seeks to address this problem by listing the types of conduct that constitute a breach of the FET standard. However, it falls short of a real improvement for three reasons. First, the list is a mere codification of already existing practice under investment law, and does not significantly limit the standard. Second, **the article codifies the 'frustration' of 'legitimate expectations'** of an investor as a breach of the standard. As one of the most far-reaching interpretations of FET, codifying legitimate expectations is not a limitation of the standard, but an expansion of it. Third, the text does not make explicit that the list is exhaustive for instance by adding the word 'only' (such as by stating 'A Party only breaches the obligation when..'). Moreover, the list is complemented with a flexibility mechanism allowing parties to discuss FET obligations, i.e. the list can be amended by the Committee which would expand the scope of the standard.

Furthermore, Article 2.4 (6) contains **an explicit umbrella clause** that elevates all private contracts of a state and its entities with regards to an investment at the level of treaty obligations. By making contracts automatically enforceable through international arbitration, it avoids dependence on the domestic court system in the host country. In other words, an investor in a town or a city will have the choice to sue the local regulator in domestic courts or to sue the host State in an international investment regime. This constitutes an additional legal loophole compared to the FET clause under CETA (Article 8.10 (4)) which does not provide for an automatic breach of international law, but only in cases where the Tribunal finds that the Party acted inconsistently.

An umbrella clause is a legal arrangement intended to promote regulatory stability beyond the provision of FET and protection against expropriations. It protects the so-called 'stabilisation clause' included in host government contracts whereby the host State commits itself not to change the regulatory framework in a way that affects the economic equilibrium of the project, and to compensate the investor if it does so. This means that Article 2.4 of EUSIPA provides for an even stronger protection for the investor, who can use the automatically enforceable right under Article 2.4 (6) in case of breach of contractual commitment, but also the 'frustration' of 'legitimate expectations' generated by specific or unambiguous representations under Article 2.4 (3) when contractual relationship of that sort cannot be proven.

- Protection against direct and indirect expropriation

Under international law, the sovereign right of host States to expropriate assets and to regulate activities within their jurisdiction is subject to conditions. Namely, takings must be for a public

purpose, in a non-discriminatory way, on the basis of due process, and against the payment of compensation. These requirements are usually spelled out in very broad terms and it results from an investor point of view that almost any law or regulation can be considered an indirect expropriation when it has the effect of reducing profits.

While the definition of indirect expropriation under Article 2.6 of EUSIPA attempts to offer a shield against some investor challenges of regulatory measures, by applying only to “non-discriminatory measures” that protect ‘legitimate’ public welfare objectives and to measures that do not ‘appear manifestly excessive’, the clause merely invites additional scrutiny of domestic policies by private investment lawyers. More preferable language would be to exempt all measures that aim or contribute to the public interest, such as environmental, social, health, or consumer protection. Otherwise, it is very easy for a Tribunal to qualify a measure as being ‘manifestly excessive’, without even need to underline and provide alternative measures. The recent ruling in *Bear Creek v. Peru* demonstrates the ineffectiveness of clauses seeking to refine the definition of investment protection standards. That case was based on the FTA between Canada and Peru, which contains provision seeking to clarify the meaning of indirect expropriation. As the Tribunal’s decision demonstrates, these provisions merely invited the panel to delve even more deeply into scrutiny of legitimate domestic public policies.[11]

- Non-discrimination

National treatment under Article 2.3 of EUSIPA requires that foreign investors be granted no less favourable treatment than the one granted to domestic investors “in like situations”. This means that better treatment of foreign investor is allowed, yet domestic investors are not afforded the same protection. Unlike CETA, Article 2.3 (2) of EUSIPA provides a list of exceptions. However, it very unlikely that these exceptions will pass the so-called “necessity test”. Practically, such test calls for an absence of any discrimination when determining the necessity of the measure to protect the public goal. The Tribunal will thus consider whether the measure taken by a democratic government (EU or Singapore) was the least discriminative towards investors among all the measures which could have been taken for the public interest, including the option of not regulating. This is highly problematic since the Tribunal may consider the measure discriminative even though it might be the only appropriate measure in a specific national legal context, or in light of other considerations (social, environmental, cultural, etc.) for longer term specific goals in a given country. In other words, the Tribunal will reassess a decision taken by a democratic body, but only through the lens of international investment law. At the EU level, this creates issues for certain Member State measures that are by nature “discriminative”, such as incentives for renewable energy instead of fossil fuel, or when applying the precautionary principle, enshrined in EU treaties.

It is worth noting that, unlike CETA, EUSIPA does not contain a provision on most-favoured nation (MNF), which requires non-discrimination between foreign investors and has led in the past to allow investors to "import" more favourable rights from other treaties signed by the host State.

[11] *Bear Creek Mining Corp. v. Republic of Peru*, Award of 30 November 2017

## 2.3. Responsible investment

The definition of covered investor and covered investment is key to determine the scope of the agreement. However, EUSIPA **fails to define these terms in a way that would only allow responsible investors to bring claims**.

First, the notion of "investment" under Article 1.2 (1) of EUSIPA is very broad and covers "every kind of asset" under direct and indirect control of an investor. This provides Tribunals broad latitude in deciding whether to hear a case and makes it difficult for host States to know which types of investment are actually protected. Moreover, the provision does not exclude certain types of assets, such as portfolio investment, government bonds and debts securities. For example, the inclusion of portfolio investment in investment treaties means that the host State has "a duty of protection to unascertainable holders of these instruments whose identities would continuously change".[12] An essential feature of portfolio investments is that they can be withdrawn at any time, notably to anticipate adverse fluctuations. This calls into question the value of such investment in view of the financial crises that have been precipitated in the past through the sudden exodus of portfolio capital. The agreement should thus explicitly exclude portfolio from its scope.

An exhaustive list of covered investments, an enterprise-based definition and social, environmental or legal thresholds would have ensured that only selected types of investment are protected under the agreement. Furthermore, the agreement does not contain a requirement on the quality of the investment, notably that the investment will contribute to achieving sustainable development goals.

Second, the notion of "investor" under Article 1.2 (2) to (5) of EUSIPA attempts to limit treaty shopping and abuses by mailbox investors by limiting applicability to "substantive business operations", but the meaning of this concept is left open to interpretation by Tribunals. Moreover, the large majority of claims are brought by corporations, and the nature of their corporate organisations, their ability to move business around the globe and the fact that the concept of corporate nationality can be manipulated by lawyers has made corporate claims more complex from the jurisdictional point of view.

Article 3.7.5 of EUSIPA (conditions to submit claims) attempts to prevent claims from investors who "acquired ownership or control of the investment for the main purpose of submitting the claim under this Section". However, it is unclear on the basis of which criteria the Tribunal will determine whether the ownership was acquired for the main purpose of submitting a claim. The Tribunal enjoys considerable freedom in the interpretation of criteria, which further opens the door to subjectivity. Thus, it is unlikely that a Tribunal will dismiss a claim arising in such situation.

Finally, Article 2.1 (scope of investment protection) of EUSIPA attempts to deprive illegal investments of treaty protection by requiring that a covered investment is inter alia "made in accordance with the applicable law". This should be strengthened by a 'clean hands clause' that would aim to dismiss any claim regarding an investment or an investor that violates core EU values, or that has violated host State law or international standards of responsible investment.[13]

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[12] M. Sornarajah, "The International Law on Foreign Investment", Cambridge, 2010, p 197

[13] An example of clean hands clause can be found in the Model Text for the Indian Bilateral Investment Treaty, Article 11: "(i) Investors and their investments shall comply with all laws, regulations, administrative guidelines and policies of a Party concerning the establishment, acquisition, management, operation and disposition of investments", https://www.mygov.in/sites/default/files/master_image/Model%20Text%20for%20the%20Indian%20Bilateral%20Inves

Moreover, there is no explicit corruption carve-out as the one under Article 8.18(3) CETA, which provides a list of reasons for excluding investors from ISDS, notably “fraudulent misrepresentation, concealment, corruption or conduct amounting to an abuse of process”. As a result, it would ensure that only investors with ‘clean hands’ can bring a claim under the agreement, and that for example Singaporean or European investors which have been charged with tax evasion or corruption could not use the ICS system against a sovereign State.

## 3. Regulatory chill

Vague provisions subject to far-reaching interpretation, combined with the intrinsic nature of the investor-state arbitration system, have raised serious concerns over a regulatory chill effect: the idea that the obligation to pay high compensations for regulatory change may make it more difficult for host States to regulate in socially desirable areas such as human rights or environment protection - including to comply with their evolving international obligations. Article 3.18 of EUSIPA attempts, but fails to effectively prevent a potential regulatory chill effect.

On the one hand, Article 3.18 excludes the award of punitive damages and limits damages to monetary damages and restitution of property at market value. On the other hand, it fails to clarify that ‘the loss suffered by the investor’, which will have to be compensated for, does not include expected profits. This is relevant in light of claims brought in relation to investor’s legitimate expectations. The award of damages indeed regularly includes speculative assessments of future value of the company and, as a result, decisions by Tribunals to condemn a law or regulation effectively become a form of State-backed insurance against regulatory change - to be determined by the Tribunal.[14] **Awards should be limited to cover only the value of proven economic damages resulting from the breach of the agreement.**

## Conclusion

We have arrived at a crucial moment where it is time for the EU to fundamentally rethink its investment protection policy. First, because of the urgent necessity to shape investment policies in line with EU values and in a way that would maximize the contribution of cross-border investments to the achievement of sustainable developments goals. Second, because it has become increasingly difficult to justify ISDS/ICS; it is losing political support even from countries among its strongest proponents.

A growing number of international investment disputes over sensitive policy issues, such as public health or the environment in the recent years, have prompted States to reconsider the investment protection provisions contained in their BITs. This trend is taking place in both developed and developing parts of the world, with EU significantly lagging behind. For instance, the US and Canada have already determined to phase out ISDS mechanism from their disputes under the new NAFTA Treaty. India has made considerable changes to their own BITs, by requiring the exhaustion of local remedies for a period of five years prior to the commencement of investment

tment%20Treaty.pdf. Inspiration could also be taken from Article 8.18(3) of CETA by expanding the list of reasons for excluding investors from ISDS (“fraudulent misrepresentation, concealment, corruption or conduct amounting to an abuse of process”) to human rights abuses, violations of national or international environmental, social, consumer, or labour laws

[14] In cases decided in favour of the investor, the average amount claimed as of the end of 2016 was $1.4 billion, the average amount awarded was $545 million, plus interest. See UNCTAD (2017a), Investor-state dispute settlement: Review of developments in 2016, IIA Issues Note

arbitration proceedings. South Africa, on the other hand, has taken a different approach, by developing a new investment protection model that would ensure government's right to regulate in the public interest, as well as the equal treatment of both foreign and domestic investors. The new South Africa model also provides for a settlement of investment disputes through domestic means, such as mediation and access to local courts, and in certain cases a state-to-state arbitration, when the domestic courts did not provide a satisfactory investment protection. This shows that in different parts of the world, States are seeking for more fair and just systems of investment protection, and are abandoning the obsolete mechanism of ISDS and vague provisions of BITs that fails to protect rights and interests of all stakeholders.

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Brussels and Warsaw. We are activist lawyers working at the interface of law, science and policy. Using the power of the law, we develop legal strategies
and tools to address major environmental issues.

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