

THE FIRST AMENDMENT TO THE JAPAN-ASEAN EPA AND WHY IT MATTERS

Introduction

On 15 June 2020, Japan notified the member states of the Association of South East Asian Nations (**ASEAN**) of its formal legal adoption of the First Protocol to amend the Japan-ASEAN Economic Partnership Agreement (**JAPEA**). Amongst other things, the First Protocol introduces an Investment Chapter into JAPEA, as Article 51 of Chapter 7 (**JAPEA Investment Chapter**). The JAPEA Investment Chapter is intended to promote and protect investments between investors from Japan and the ASEAN Member States (Brunei, Cambodia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam). It contains wide-ranging investment protections for investors from these jurisdictions and includes an investor-State dispute settlement (**ISDS**) mechanism. But the ISDS provisions have a twist – there are various novel features and innovations that show State practice in the area of ISDS is continuing to evolve and that Asian nations, increasingly experienced with ISDS, are at the forefront of these developments.

New protection for investors investing in Japan or an ASEAN member state

Who and what is covered?

The JAPEA Investment Chapter protects "*investors*" operating in the territory of a JAPEA party (Article 51.2(d)), including citizens from, or legal persons incorporated in, Japan or the ASEAN Member States. To be covered by the available protections, investors must have taken active steps to initiate any applicable approval process for foreign investment in the host State concerned.

"*Investments*" protected under the JAPEA Investment Chapter are defined widely and include property rights, shares, stocks, bonds, debentures, intellectual property rights, licences, rights under contracts and other assets. However, the JAPEA Investment Chapter indicates that the investment may have to be "*admitted, according to [a Party's] laws, regulations and national policies*".

ISDS cases illustrate that admission requirements of this kind provide States with fertile ground for jurisdictional objections, if a dispute arises. The host will often rely on such provisions to raise jurisdictional objections on the basis that the investment lacked a necessary regulatory approval or was tainted by some other alleged defect under local law, thereby depriving it of the status of a protected "*investment*" under the treaty. To mitigate this risk, amongst other things, investors need to ensure they have taken appropriate local law advice when setting up their investment as well as completing appropriate legal due

Key Takeaway

Wide-ranging investment protections under the Japan-ASEAN EPA:

- In force 1 August 2020; and
- Enforced by arbitration.

diligence. Investors should take care to secure original copies of all licences, permits and other approvals they receive from the host government in relation to their investment. If there is any doubt as to the authenticity of a government document, the investor should take steps to have that document verified.

What protections are available?

The JAEPA Investment Chapter grants the following key protections to covered foreign investors and investments:

National treatment (Article 51.3): this prohibits discrimination based on an investor's nationality. In other words, Japanese investors in an ASEAN Member State must enjoy the same treatment the host State grants to local investors.

Protection from expropriation and nationalisation (Article 51.9): State parties may not unlawfully expropriate or nationalise foreign investments covered by JAEPA except for a public purpose, in accordance with due process on a non-discriminatory basis and accompanied by payment to the investor by the state of "*prompt, adequate and effective*" compensation.

Fair and equitable treatment (FET) (Article 51.4): Investors and investments must be treated in a fair and equitable manner by the host State, which prevents discriminatory treatment and governmental measures that violate the investor's legitimate expectations. However, the FET standard in the JAEPA is limited to the "*customary international law*" standard, which arguably offers a lower standard of protection than other types of FET clauses found in investment protection treaties.

Full protection and security (FPS) (Article 51.4): the governments of Japan and ASEAN must provide physical protection (e.g. police or military protection) to covered investments, which must be at least the same as the protections provided to host State nationals. Notably, this protection is also linked to the "*customary international law*" standard.

Prohibition of performance requirements (Article 51.5): this Article prohibits a host State imposing conditions on the management or operation of covered investments such as import/export quotas or requirements to use locally produced goods or materials.

Free transfers (Article 51.11): subject to certain limitations, investors are free to transfer capital, profits, interests, royalties, fees, dividends, technical assistance fees, management fees or other cashflows related to their investments.

Limitations and Restrictions

There are various limitations and restrictions in the JAEPA Investment Chapter. For example, government measures required to preserve national security or public health are carved out from the scope of the expropriation provisions. Investors wishing to ensure they can take the full benefit of the protections offered by this treaty, or make a claim under it, should ensure they take advice regarding the application of the JAEPA to their investments and how best to approach its limitations and restrictions.

A new generation of ISDS clauses?

The JAEPA Investment Chapter contains an ISDS mechanism (Article 51.13). Subject to various exclusions, the ISDS mechanism enables investors to submit investment disputes to investor-State arbitration under the ICSID or UNCITRAL

Rules. The principal effect of the ISDS mechanism is to make the substantive protections granted by the JAEPA Investment Chapter directly enforceable by investors, without the need for representation or assistance from the government of their home State. The ISDS clause is broadly effective but contains some novel and noteworthy features as well as some important exclusions, including:

1. Investors may submit investment disputes under the JAEPA Investment Chapter to the courts or administrative tribunals of the host State. Although it is not unusual for investment treaties to provide that investors may seek recourse in the host State's courts or administrative tribunals, JAEPA is novel in that it expressly contemplates that the local courts and administrative tribunals may lack jurisdiction to hear a claim for violation of the treaty (Article 51.3(7)(a)(i)).

2. Investors must choose to resolve investment disputes either through the courts or through arbitration. Once one process has been initiated by the investor, the alternative route is no longer available. This type of provision is known as a "*fork-in-the-road*" clause. Investors need to be aware of this clause and the consequences that commencing local court proceedings (or administrative appeals) may have on their ability to make claims through ISDS.

3. Where an investor seeks to refer an investment dispute with Indonesia or the Philippines to ICSID arbitration, a further written consent is required from the respondent State before ICSID arbitration will be available (this reflects a similar reservation made by the Philippines in the ASEAN Comprehensive Investment Agreement). Significantly, if Indonesia or the Philippines does not consent to ICSID arbitration, the investor may still refer the dispute to other forms of ISDS (including arbitration under the UNCITRAL Rules).

4. Thailand only consents to arbitration with foreign investors where there is an "*existing international agreement*" (between Thailand and the investor's home State) containing Thailand's consent to arbitration. The JAEPA Investment Chapter also places a similar constraint on Thai investors' access to arbitration against other JAEPA States. This is an unusual provision – not least because it may be read as purporting to limit the consent of Thai *investors* (Article 51.13(9), Note 2), who, unlike the Kingdom of Thailand, are not parties to the treaty.

5. The JAEPA Investment Chapter contains provisions that deal with issues that are more commonly left to the rules of arbitration incorporated into the treaty, such as the ICSID Arbitration Rules or UNCITRAL Rules (Article 51.13(14) – (16)). For example, it contains provisions on timing of jurisdictional and admissibility objections, the right of parties to strike out a claim for manifest lack of legal merit and guidance on the allocation of costs.

6. The ISDS clause provides that, during an arbitration, the arbitral tribunal or a disputing party may request an issue of interpretation to be referred to a Joint Committee consisting of representatives of Japan and each ASEAN Member State. Joint Committee decisions are binding on the tribunal (Article 51.13(20)).

In summary, the ISDS clause in the JAEPA Investment Chapter contains certain novel and innovative provisions which demonstrate that many of the State parties to the treaty are now well experienced in the theory and practice of ISDS. Overall, these innovations are likely to make it harder for investors to bring successful claims but there can be no doubt that the unanimous intention of the drafters was to ensure that investors still have some right of recourse to ISDS, notwithstanding the different attitudes of the governments concerned. While arbitration may be the last resort, the fact the JAEPA now grants investors a

clear right to arbitration should, at the very least, give investors leverage in negotiations with host governments. The JAEPA Investment Chapter is therefore an important and sophisticated new feature in the Asian investment treaty landscape.

Further Information

Extensive guidance on investment treaty structuring is available from Clifford Chance. This note is an overview only and is not legal advice. For further explanation on the protections available under the JAEPA, or if you would like to know more about using investment treaties to protect your international investments more generally, please contact one of the individuals listed below.

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